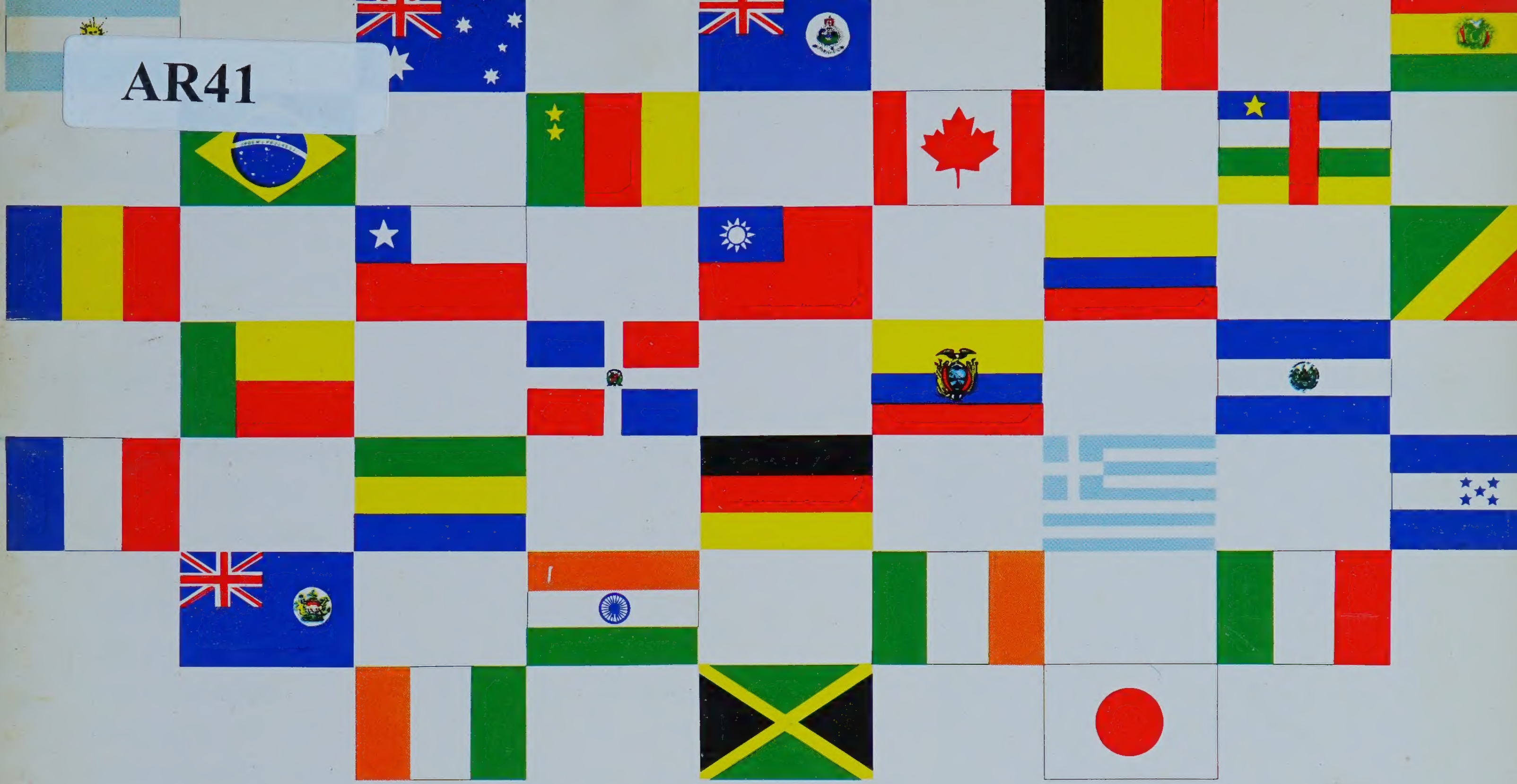
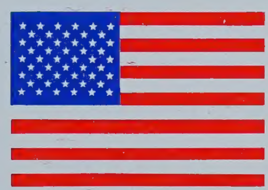
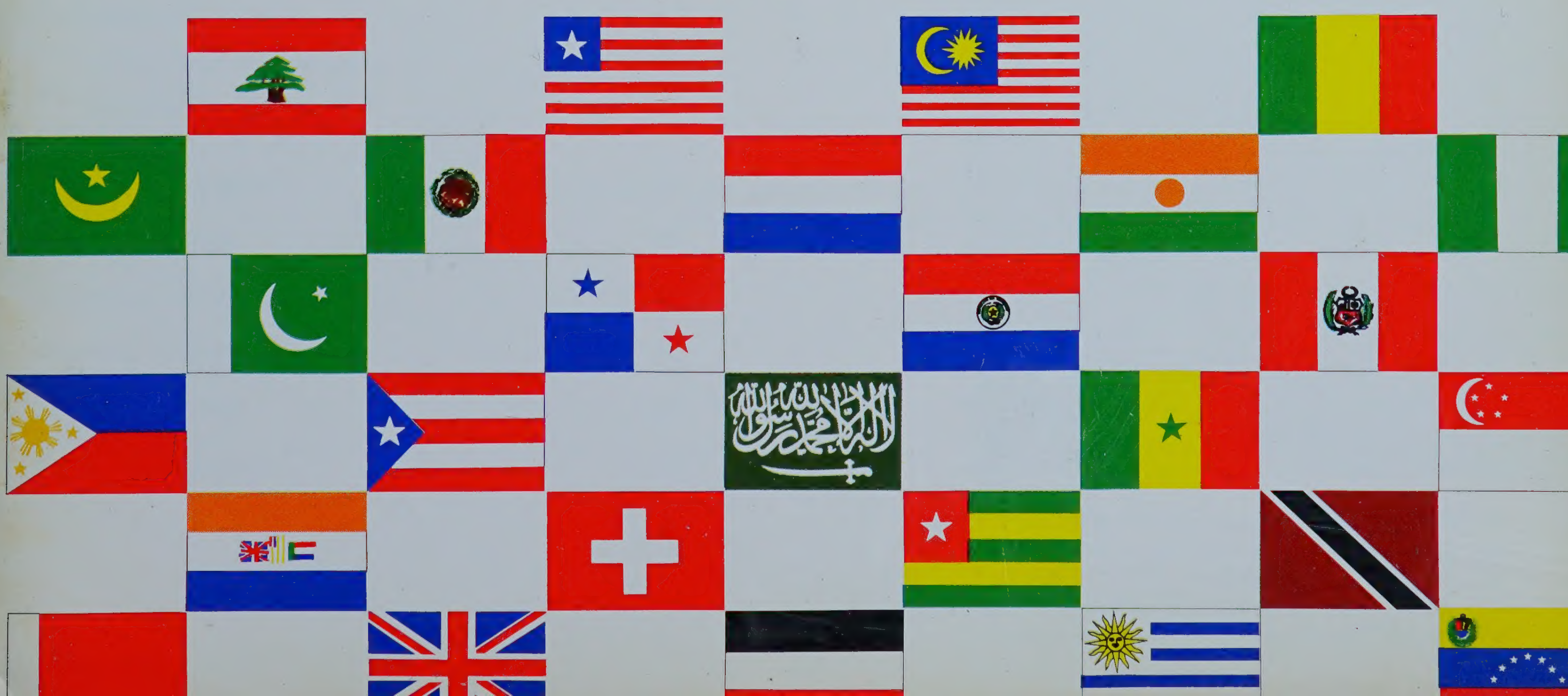




FIRST NATIONAL CITY BANK

Annual Report 1966



Directors and Trust Board

GEORGE F. BAKER, JR.* *Trustee, George F. Baker Trust*

DANA T. BARTHOLOMEW* *Vice President and Chief Financial Officer, Alcan Aluminium Limited*

WILLIAM M. BATTEN *Chairman, J. C. Penney Company, Inc.*

JOHN E. BIERWIRTH *Chairman of the Board, National Distillers and Chemical Corporation*

CHARLES M. BRINCKERHOFF *Chairman of the Board, The Anaconda Company*

WILLIAM H. CHISHOLM* *President, Oxford Paper Company*

PERCY CHUBB, 2nd *Chairman, Chubb & Son Inc.*

FREEMAN J. DANIELS* *Perkins, Daniels & McCormack*

HUNT T. DICKINSON* *405 Lexington Avenue*

ROBERT W. DOWLING* *Chairman, City Investing Company*

FREDRICK M. EATON *Shearman & Sterling*

R. GWIN FOLLIS *Chairman of the Board, Standard Oil Company of California*

J. PETER GRACE *President, W. R. Grace & Co.*

GORDON GRAND* *Chairman of the Board and President, Olin Mathieson Chemical Corporation*

JOSEPH A. GRAZIER *Chairman, American Radiator & Standard Sanitary Corporation*

MICHAEL L. HAIDER *Chairman, Standard Oil Company (New Jersey)*

HOWARD C. HARDER* *President, Corn Products Company*

H. MANSFIELD HORNER *Chairman, United Aircraft Corporation*

AMORY HOUGHTON *Honorary Chairman of the Board, Corning Glass Works*

AMORY HOUGHTON, JR.* *Chairman of the Board, Corning Glass Works*

GEORGE P. JENKINS *Chairman of the Finance Committee, Metropolitan Life Insurance Company*

JOHN R. KIMBERLY *President, Kimberly-Clark Corporation*

J. HOWARD LAERI* *Vice Chairman*

ROGER MILLIKEN *President, Deering Milliken, Inc.*

GEORGE S. MOORE *President*

CHARLES G. MORTIMER *Chairman of the Executive Committee, General Foods Corporation*

ROBERT S. OELMAN *Chairman, The National Cash Register Company*

WILLIAM F. OLIVER* *President, American Sugar Company*

RICHARD S. PERKINS *Chairman of the Executive Committee*

CLIFTON W. PHALEN *Chairman of the Executive Committee, New York Telephone Company*

JAMES S. ROCKEFELLER *Chairman*

CHAS. H. SOMMER *President, Monsanto Company*

WILLIAM C. STOLK *Director, American Can Company*

ALAN H. TEMPLE* *399 Park Avenue*

HULBERT W. TRIPP* *Senior Vice President*

J. ED. WARREN* *Consultant, 1271 Avenue of the Americas*

LEO D. WELCH *Former Chairman of Standard Oil Company (New Jersey) and of Communications Satellite Corporation*

ALBERT L. WILLIAMS *Chairman of the Executive Committee, International Business Machines Corporation*

JOSEPH C. WILSON *Chairman and Chief Executive Officer, Xerox Corporation*

ROBERT WINTHROP* *Wood, Struthers & Winthrop*

HOWARD C. SHEPERD *Chairman Emeritus*

**Member Trust Board*

FIRST NATIONAL CITY BANK

ANNUAL REPORT 1966

Contents

Highlights of 1966 2

Message from Management 3
Outlook for the Economy 4
Outlook for the Bank 5

Financial Summary 6
The Year's Earnings 6
Losses on Loans 6
Security Profits and Losses 6
Loans and Investments 8
Deposits 8

Citibank's Specialized Services 10
A Division of Specialists 10
Meeting New Needs 12
Financial Engineering 12
Full-Service Banking for Business 13
Specialists in Personal Services 14
New International Services 16
Expansion Abroad 16
Trust and Investment Specialists 17
Behind the Lines 18

Citibankers in Action 19
Citibankers in Training 19
Community Participation 22

Affiliated Companies 23

Domestic Offices 24

Overseas Offices 26

Financial Statements 28

Ten Year Record 32

Senior Management 33

Growing Plans. *Data processing and financial district operations will be moving into this 24-story building at 111 Wall Street when it is completed in 1968. The new space will enable Citibank to consolidate various activities which are presently scattered at a number of locations.*

IN 1966, YOUR BANK

- achieved record net operating earnings of $105 million, 12% above 1965, and equivalent to $3.94 per share.

- increased the annual dividend rate from $1.60 to $1.80 per share and paid shareholders $47 million from the year's earnings.

- gained 8% in loans, in total assets, and in deposits.

- offered new customer services, including—

  —our unique Commingled Investment Account for smaller investors,

  —Travel Selection Centers in eight New York offices,

  —"Checking Plus"—a regular checking account plus an individual line of credit.

- opened 13 new branches for the convenience of customers in the New York area, making a total of 164.

- added 18 new offices overseas, bringing the total to 195 in 60 countries on six continents.

To Our Shareholders, Customers, and Staff:

In 1966, the sixth consecutive year of business expansion, a sharp rise in defense spending, superimposed on a surging civilian economy, produced inflationary pressures and the highest interest rates since the early 1920's. Toward year end, in response to efforts of the monetary authorities to curb the boom and combat inflation, there were signs of some slowdown in activity and easing in some commodity prices and in interest rates.

Banks' liquidity positions were under great pressure during the year as demand for loans outran the supply of loanable funds. Under the ceilings imposed by the Federal Reserve on the interest rates banks may pay on various types of savings and other time deposits, banks found it difficult to compete for funds against higher yields available in the market. Consequently, total time deposits leveled off after August while loan demand continued strong.

These developments were naturally reflected in the operations of First National City Bank. Total assets and deposits rose to new highs, but the increases were not as large as in 1965. Thanks to a significant improvement in the yield on our expanded loan portfolio, income from loans rose considerably more than interest payments on deposits.

As a result, net operating earnings of the Bank were up 12% over the previous year. In June the annual dividend rate was raised from $1.60 to $1.80 per share.

It was a year of progress for the Bank in many directions. Operating efficiency has been improved through greater utilization of automated systems. Our domestic and overseas networks of branches and affiliates have been further expanded. Trust business has continued to grow. More new services have been introduced. This report presents the story of these varied activities.

It has been a difficult period for lending officers because, in common with most banks, we have not been able to meet all demands for credit. We have naturally done our best to fulfill our obligations to customers, but it has frequently been necessary to cut back or decline loan requests of one kind or another. To those whom we have not been able to accommodate fully, we express our regret and look for another opportunity to serve when credit conditions have eased.

The year has seen a number of changes in our Board of Directors. Joining the Board were Joseph C. Wilson, chairman and chief executive officer of Xerox Corporation; Albert L. Williams, chairman of the Executive Committee, International Business Machines Corporation; and Fredrick M. Eaton, partner in the law firm of Shearman & Sterling. They succeed Reginald B. Taylor, C. Sterling Bunnell, and Charles C. Parlin.

William H. Chisholm, president of Oxford Paper Company, and Gordon Grand, chairman of the board and president of Olin Mathieson Chemical Corporation, were appointed to the Trust Board. Howard C. Sheperd, former chairman of the Bank, was appointed chairman emeritus.

The continuing active interest of our shareholders is welcomed. More than 18,000 responded to survey questionnaires regarding our annual report and the brief quarterly reports that accompany dividend checks. We were pleased to find that the overwhelming majority regards these reports in their present form as being informative and useful.

Top Management. *Richard S. Perkins, chairman of the Executive Committee; James S. Rockefeller, chairman; and George S. Moore, president.*

Citibank's achievements have not come about accidentally or automatically. They reflect the combined efforts of our 24,000 staff members around the world, and again we express our appreciation for their loyalty and cooperation.

Outlook for the Economy

The economy should continue to grow in 1967, but at an appreciably slower rate than in 1966. A slowdown began to emerge in the closing months of the year. It reflects to a considerable extent the success of monetary restraint in cooling off an overheated economy. Because there is normally some lag in the impact of changes in monetary policy, we have probably not yet seen the full effect of the severely restrictive policy pursued during much of 1966. Still, the underlying growth forces are strong and it is possible that within the year vigorous expansion may be resumed.

For more than a year now, consumer budgets and money incomes have been squeezed by more rapidly rising prices and higher tax payments. Consumers have slowed their buying of durable goods, such as automobiles and appliances. While dollar outlays for nondurable goods and services have done better, much of the increase has reflected higher prices.

New housing starts, which were sharply reduced last year from the 1965 level, are expected to show some improvement as mortgage money becomes more readily available. It will take time, however, for mortgage lenders to recover fully from the severe liquidity squeeze of 1966.

In these circumstances there is naturally a good deal of uncertainty about the outlook for sales and profits. Further caution is warranted by rapidly mounting inventories, financing difficulties, and the trend toward higher wage settlements. Surveys indicate that plant and equipment expenditures in 1967 will be up from last year, but the increase now expected would be the smallest since the present expansion began six years ago.

Government spending is likely to rise sharply during the year ahead. Nevertheless, military outlays are not expected to stimulate the economy as much as they did in 1966, barring a substantial enlargement of the war in Vietnam. State and local government spending will continue to climb.

Toward year end, the monetary authorities responded to the slackening pace of business expansion by making funds somewhat more easily available. There is little doubt that we are moving from the severe credit dislocations of 1966 toward a more orderly flow of funds and somewhat lower interest rates.

The record of U.S. international payments in 1966 was a mixed one. The trade surplus fell as imports climbed rapidly in response to buoyant domestic conditions. The marked improvement in capital movements was attributable in part to control and tax measures and in part to the sharp rise in interest rates. The direct foreign exchange costs of the war in Vietnam increased. The deficit, as conventionally measured, remained at $1⅓ billion in 1966, unchanged from 1965. With a deficit of this size, although much reduced from earlier years, the United States may still be supplying the world with more dollars than other nations want and will retain willingly.

The outlook for the balance of payments is uncertain. Slower domestic growth may halt the deterioration in the trade surplus, but a decline in inter-

est rates in the United States could mean a reversal of the inflow of funds that proved helpful last year.

For 1967, much will depend on our ability to hold down production costs and thus preserve our competitiveness in world trade. Much will also depend on the confidence of our own people as well as of nations abroad in the soundness of our economic and financial policies. When the danger of inflation has diminished, the chances for continuing balanced economic growth are excellent.

Outlook for the Bank

We anticipate some further growth in our deposits over the coming year, but it is difficult to say how much. It seems safe to say deposits at overseas offices will continue to expand. However, the trend of net demand deposits in New York has been flat for a long time and this could easily be the case again in 1967. At this juncture it is unclear what will happen to domestic savings and other time deposits.

For years the Bank has sought actively to attract time deposits in order to meet customers' needs for credit. Our ability to compete for these funds, however, is greatly influenced by developments in the money market and by regulations on the interest rates banks are permitted to pay depositors. These factors caused an actual contraction of our time deposits in New York during the latter part of 1966.

At the present time, these factors do not appear to be as threatening as they were last summer. We are hopeful that the attrition of savings deposits has by now run its course and that, over the coming year, we should be able to compete effectively for domestic savings and other time money.

With an increase in deposits, and assuming no more than a moderate slowdown in economic activity, we would expect some further expansion in our loan portfolio. The tightness of credit in the past year has caused the postponement of some borrowing and has built up a backlog of loan demand. Our expanding system of domestic branches will enable us to continue to increase our personal instalment loans and mortgage loans to residents of the New York metropolitan area.

We enter the new year with a larger loan portfolio and a higher average rate of return on loans than a year ago. Even if there should be some easing of credit conditions, we would not anticipate much decline in the yield on our loans. Total revenues of the Bank should therefore increase, though less than in 1966.

Similarly, expenses will continue to grow but probably at a slower pace than last year. Three fourths of the increase in operating expenses in 1966 was in interest paid, and the rise in this major category of expense should be considerably smaller in 1967.

All in all, it should be another good year for First National City Bank—for shareholders, for staff members, and for the customers we serve.

Richard S. Perkins
Chairman of the Executive Committee

George S. Moore
President

James S. Rockefeller
Chairman

Financial Summary

The Year's Earnings

Net operating earnings of the Bank and its wholly-owned subsidiaries increased in 1966 to a record $104,890,000, up 12% over the preceding year. Earnings per share were $3.94 compared with $3.52 in 1965.

Total operating income rose $85 million, up 17%. Three fourths of this increase consisted of additional interest on loans. Loan volume was up, and for the first time in six years, there was a significant increase in domestic lending rates. The average rate earned on loans was 5.71% compared with 5.27% in 1965.

Income from securities was up $4 million. Holdings of securities were reduced to accommodate customers' needs for funds but investment yields rose more than enough to compensate.

Other income rose sharply, $16 million, due principally to higher trust income, larger earnings remitted from overseas branches, and an increase in service charges and commission income.

On the expense side, the major increase was in interest paid which was $49 million higher. This reflected higher rates on interest bearing deposits as well as some increase in the total amount of these funds.

Losses on Loans

Losses on loans are inevitable for any bank that performs its proper role in the economy. It is general practice among banks to compute net operating earnings without taking such losses into account, chiefly because they may vary so greatly from one year to another. Nevertheless, credit losses are part of a bank's earnings picture and we have regularly reported this information.

Net losses on loans in 1966 totaled $12 million. However, one should bear in mind that these losses result in a reduction in the Bank's tax bill. After taking into account the resulting tax reduction, net loan losses in 1966 were $6 million, as shown in the Statement of Earnings on page 29, which was equivalent to 7/100ths of one percent of total loans outstanding at year end.

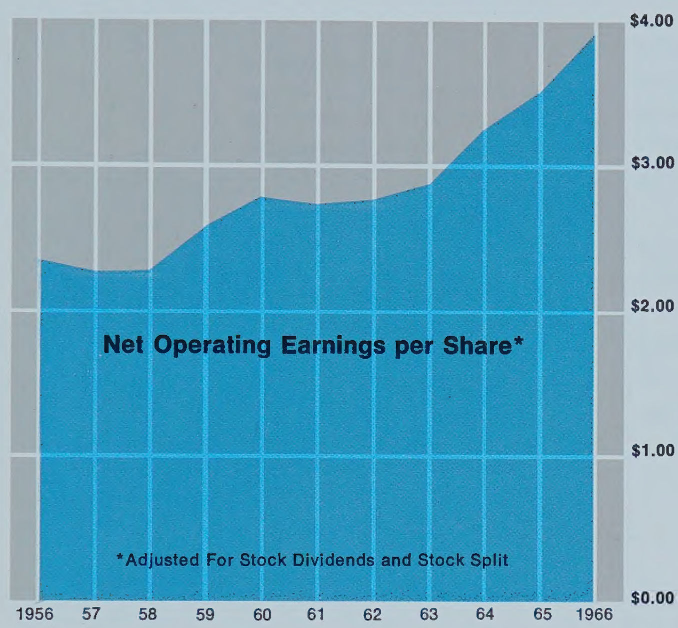
Over the past 10 years, such losses, after allowing for tax reductions, have averaged $4 million per year, also equivalent to 7/100ths of one percent of outstanding loans. They were equal to 5% of net operating earnings for the 10-year period. The percentages for the preceding 10 years were even lower.

About 37% of our net credit losses over the past decade were incurred in one year, 1960, in connection with the Cuban revolution. We sustain large losses of this kind every once in a while in our far-flung and profitable international operations and this is one reason why we have built up $317 million of reserves against possible loan losses and other contingencies.

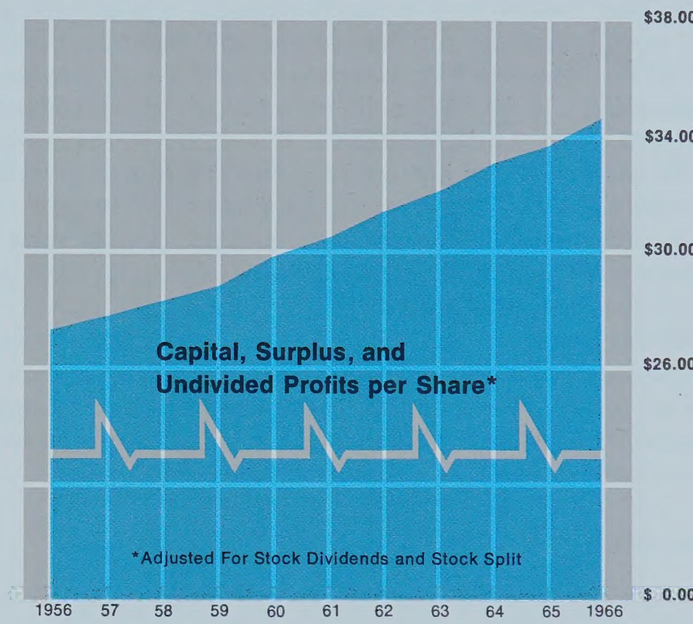
Security Profits and Losses

Similarly, profits and losses realized on sales of investment securities are not reflected in the computation of net operating earnings, but here again, it has long been our practice to report these figures. In the usual course of events, bankers expect to take losses on securities from time

Earnings Per Share

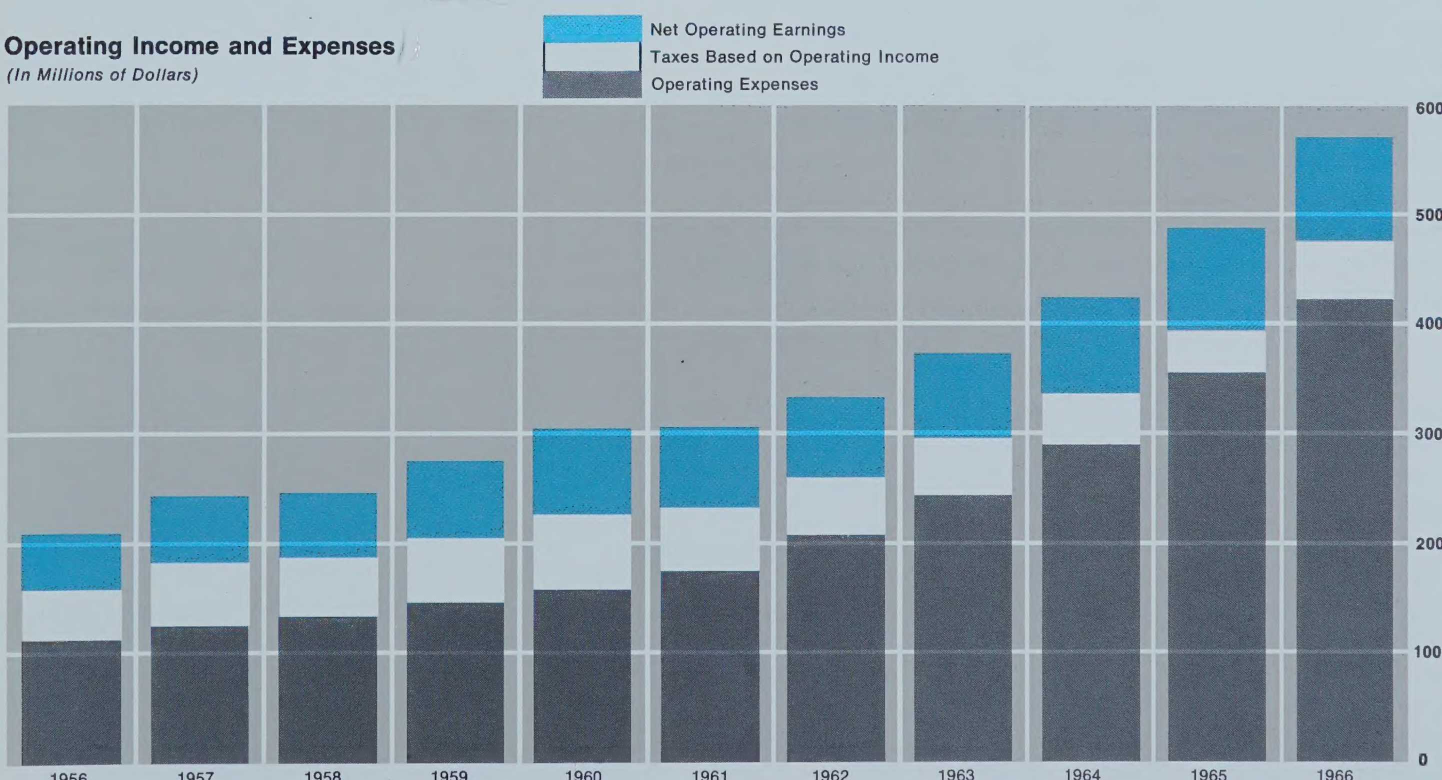


Book Value Per Share



Operating Income and Expenses

(In Millions of Dollars)



to time. When loan demand slackens, they put their funds to work in securities, even though bond prices tend to be high at such a time.

If they were to hold all such securities until maturity, bankers would rarely incur any losses in their investment portfolios. However, there are occasions when it is advantageous for a banker to sell securities at low prices and to reinvest the proceeds at the higher yields currently available in the market. There are also times when he must sell bonds at a loss in order to obtain funds to meet his customers' needs.

On the other hand, opportunities arise from time to time to realize profits from sales of securities. Over a period of years, such profits may largely offset losses.

In 1966, net losses on sales of securities, after taking tax reductions into account, amounted to $5 million. Over the past 10 years, however, after-tax security profits have exceeded losses by a small margin. But far more important, income from securities over this period has amounted to $705 million.

Loans and Investments

Loans averaged 10% higher than in 1965, reflecting strong demands for all types of credit. However, due largely to the relative scarcity of funds, the increase was only about half that of the preceding year.

On the basis of average figures throughout the year, loans amounted to 73% of deposits, the highest percentage in a generation.

The average yield on investment holdings of U.S. Governments rose from 4.00% in 1965 to 4.34% in 1966. The return on state and municipal securities increased from 3.21% to 3.47%, equivalent to 6.97% on a fully taxable basis.

The average maturity of U.S. Government obligations held at year end is 46 months. Of these securities, 50% mature within five years and all of them are due within 10 years.

Deposits

Total deposits rose to $12.9 billion at year end, a new high. Most of the increase was at overseas branches. Domestic demand deposits were higher at year end, but on average throughout the year were virtually unchanged.

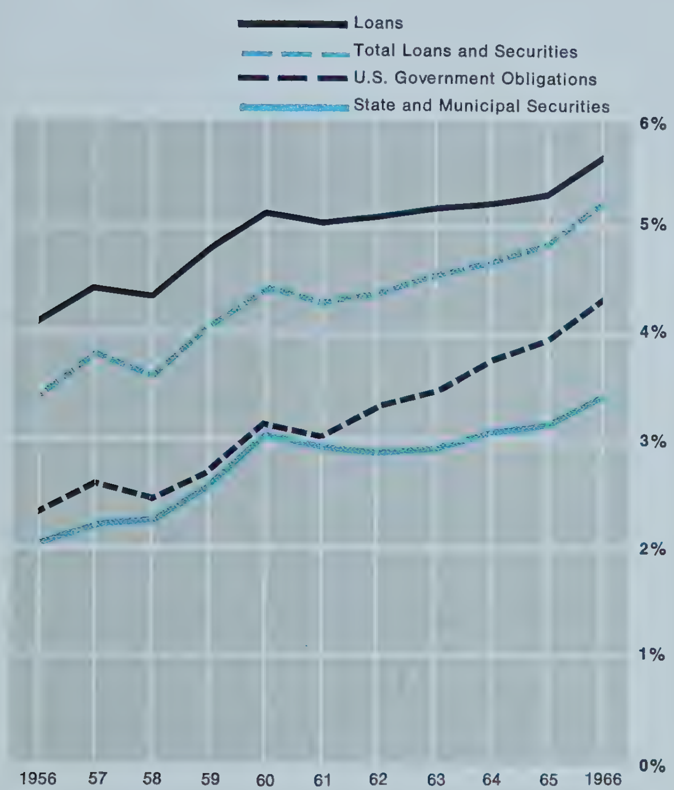
As shown by the chart on the facing page, interest bearing domestic deposits showed a notable leveling off after several years of rapid growth. High yields available on bonds and other investment media, coupled with the rate ceilings to which commercial banks are subject, made it more difficult to attract funds. Savings deposits actually declined slightly and other time deposits increased only moderately. There was some shifting from savings accounts to take advantage of the higher rates payable on other types of time deposits.

The average rate paid on all interest bearing deposits in New York rose to 4.66% from 4.12% in 1965. Savings and other time deposits now constitute 39% of our domestic deposits compared with 21% five years ago and 15% 10 years ago.

The growth in deposits at overseas offices reflects the continuing expansion of our established international business and the increasing importance of the market for Eurodollars.

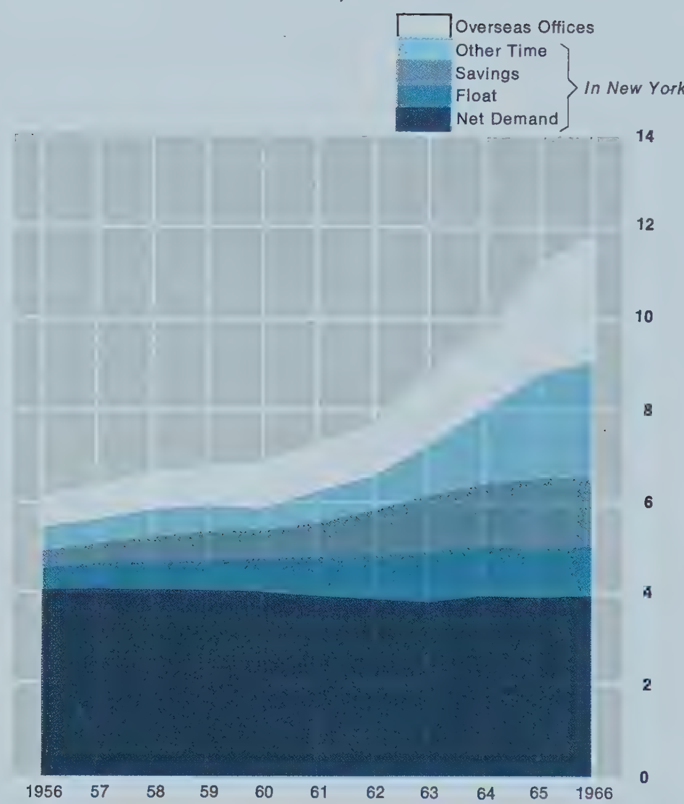
Average Annual Rate on Loans & Securities

(In New York)



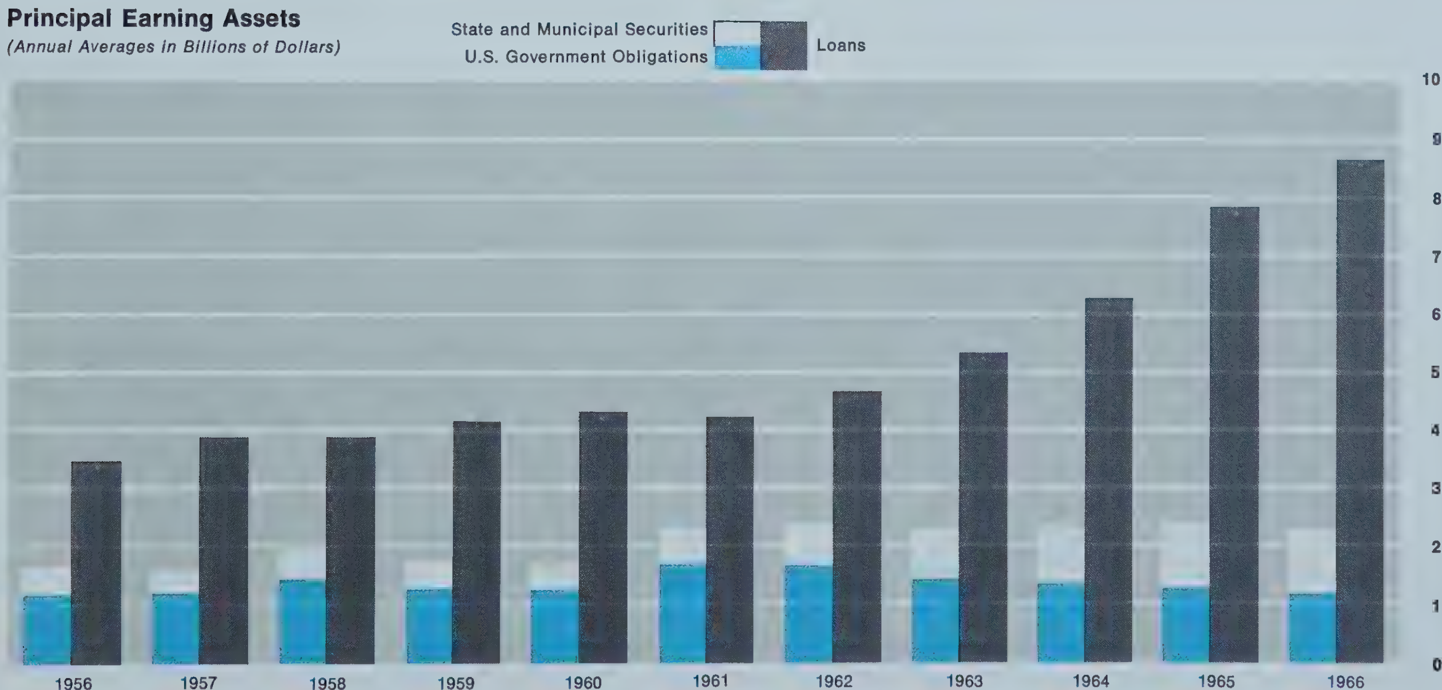
Deposits

(Annual Averages in Billions of Dollars)



Principal Earning Assets

(Annual Averages in Billions of Dollars)



Citibank's Specialized Services

First National City Bank has long made a specialty of developing services tailored to the needs of all segments of the various banking markets we serve. Each year we provide more services to more customers in more markets. Our clientele ranges from 99 of the 100 largest U.S. industrial corporations to sidewalk newsstands, homeowners, and young people attending college.

In recent years, needs for financial services have been changing rapidly and becoming both more diverse and more exacting. Our efforts to accommodate customer requirements have kept pace. Throughout the Bank, the constant emphasis is on expanding and improving our services.

The past year has been one of substantial progress in this regard. Old services were refined and new ones introduced. Training programs at all levels were stepped up. More specialists were added to our staff. Groups serving particular customer needs were enlarged and several new ones were formed. A number of these groups have been brought together to form a separate division, the Specialized Industries Division.

We are committed to the concept of the full-service bank and have found that this approach enables us to provide better as well as broader service to customers. First-hand experience in retail banking gives us a better understanding of the problems of our correspondent banks across the country. Domestic corporations expanding their foreign operations derive increasing value from the services of our network of fully staffed branches around the world.

And so it goes. Each activity supports, and is supported by, every other activity.

Seeking out new ways of being of special service to our customers has helped us to grow. Here is the story of that growth in 1966.

A Division of Specialists

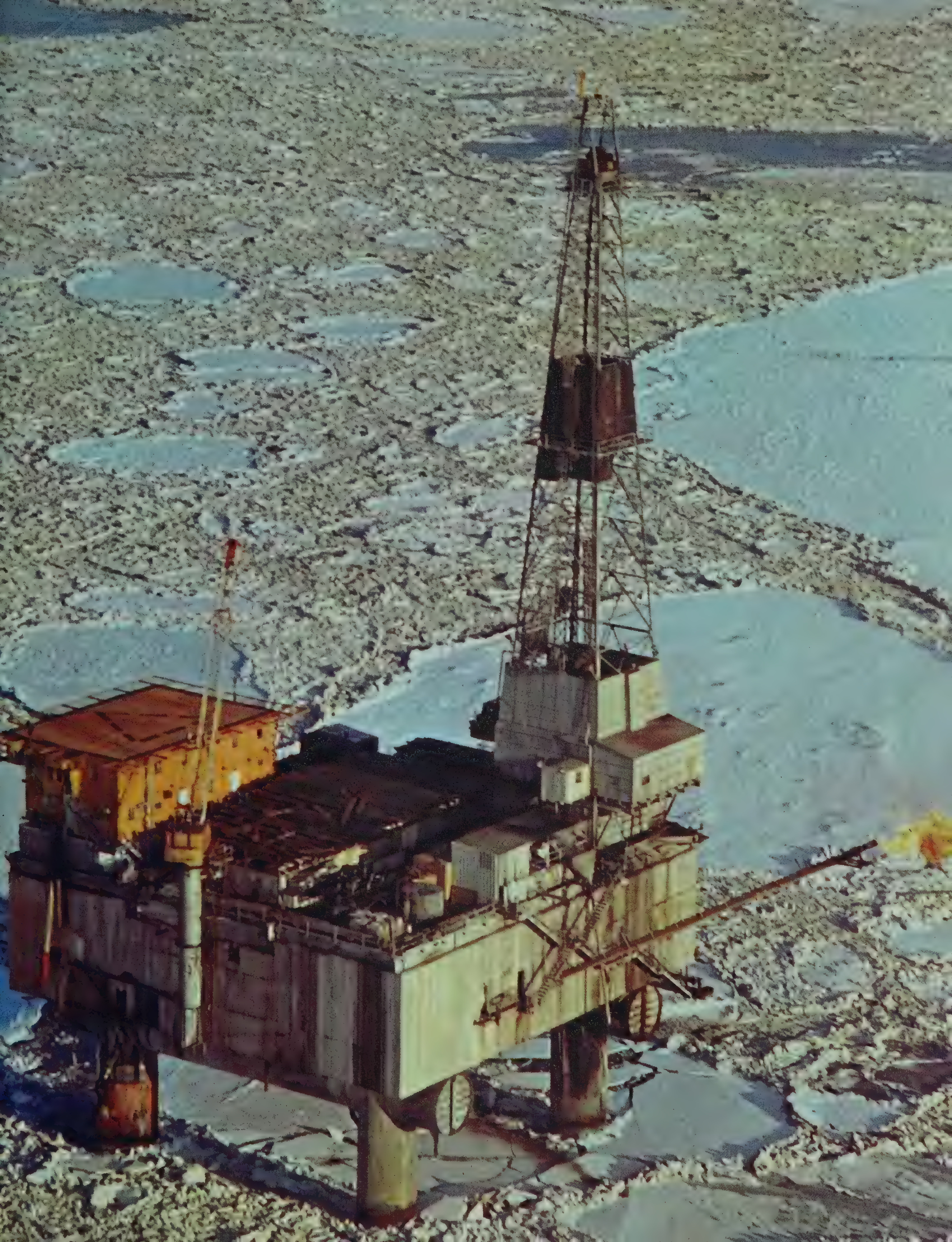
The mission of the Specialized Industries Division is to satisfy the increasingly complex needs of customers in key industries. To accomplish this, the division is organized on a functional basis rather than along the geographic lines common in the Metropolitan, National, and Overseas Divisions.

Teams of financial and technical specialists concentrate their activities in eight departments: Aerospace and Electronics, Petroleum, Minerals and Mining, Public Utilities, Equipment Leasing, Transportation, Insurance, and Wall Street and Financial Institutions. Experts in these areas analyze current and anticipated business trends and their impact on the companies affected.

Division officers directly serve all major customers in these industries regardless of their geographic location. In addition to applying the division's own expertise, they also bring the full resources of other parts of the Bank to bear on each customer's problems.

Two characteristics common to most of the industries which this division serves are dynamic change and immense capital requirements. Constant study and imagination are required to keep on top of these changes and meet customer needs with innovative financing.

Oil from the North. *Cook Inlet in Alaska is a rapidly developing area of importance to the petroleum industry and, consequently, to Citibank. We are the leading bank in the financing of the Cook Inlet Pipeline which serves offshore drilling operations in the area.*



Meeting New Needs

During the year, the Aerospace and Electronics Department applied its know-how to the unique financial requirements of aerospace, electronics, and information systems companies. Through its assistance to these customers, Citibank financed the production of hardware needed for the war in Vietnam, for supersonic flight, and for space exploration.

Advances in technology are strikingly apparent in transportation where piggyback containers that travel by rail, ship, or highway; 500-passenger jet aircraft; mammoth tankers; and vessels that will transport highway trailers across the ocean all either exist now or are close to reality. In this fast-changing industry, the Transportation Department is playing a role unknown only a short time ago.

The public utility industry has for years ranked high in terms of capital requirements. In many cases our principal function is to provide interim and term construction monies and we are also frequently consulted on the design of long-term financing programs.

In 1966 our equipment leasing activities continued to expand. Since its organization in 1964, the Equipment Leasing Department has purchased and leased equipment costing many millions of dollars, including aircraft, railroad cars, locomotives, truck trailers, computer systems, and various types of production equipment.

The Bank annually sponsors a forum on economic and investment topics for leaders of the insurance industry. The 1966 forum was attended by 182 senior executives of domestic, Canadian, and European companies.

By no means all of the Bank's groups of specialists are in the Specialized Industries Division. Indeed, there has been a strong trend toward greater specialization in all parts of the Bank. The general practitioner is becoming almost as rare in a metropolitan bank as in the field of medicine.

An example in the National Division is the group serving the requirements of correspondent banks. Each year more names are added to the roll of our distinguished correspondents of all sizes throughout the country. The annual Correspondent Bank Forum was held in the 399 Park Avenue auditorium on February 5 and was attended by more than 300 senior officers of correspondent banks.

Air, Road, and Rail Speedup. *Citibank's Transportation Department specialists provide for the financing needs of the fast-paced developments in the world of supertankers, jet liners, and highway-trailer hybrids which travel by river and sea as well as by rail.*

Financial Engineering

At ten o'clock one morning last July, two Citibank officers took their places at the head of a conference table in the midwest headquarters of a major manufacturing corporation. For two hours they conducted management through a tour of Citibank's recommendations on the financial strategy the company should follow through 1970.

These were no routine recommendations based on straight-line projections of past performance. They were, instead, the product of the Corporate Financial Advisory Department which had prepared a 32-page analysis of this company's future financial needs. The report included

projected earnings statements and annual balance sheets for the next five years produced by a computer on the basis of certain data and assumptions about the customer and his business.

The customer was told, for example, that the shortfall of cash for capital needs over the next five years would range from $80 million to $130 million, depending upon the assumptions adopted. "The most probable shortfall," said the report, "will be around $100 million." The analysis then went on with detailed financing recommendations.

Forecasting a customer's future financial requirements and evaluating the merits of available alternatives by computer is simply the latest in a long series of steps taken by the Bank in the past decade to serve the increasingly complex needs of its customers. The facilities and resources we are developing have enabled us to provide services of this type on a fee basis, and we are in the process of expanding this activity.

In addition we have developed a variety of other computer services tailored to the needs of business customers. At the present time, the Automated Customers' Services Department offers account reconcilement, demand deposit and instalment loan accounting, payroll services, and real estate collection services.

Financing Financiers. *Ever since its founding in 1812, Citibank (originally The City Bank of New York) has played a leading role in serving the special needs of the financial markets.*

Full-Service Banking for Business

Many of the officers in the Metropolitan and National Divisions who serve corporate customers in New York and throughout the country are specialists in the financial problems of leading industries in the territories to which they are assigned.

In the New York metropolitan area, we serve small businesses as well as large. One of the specialized services offered to small businesses is the term loan repayable in monthly instalments. In 1966, loans of this type totaling $30,300,000 were made to more than 6,400 small businesses.

Hubshman Factors Department offers the highly specialized services of factoring, accounts receivable financing, and time sales financing to a wide range of industries. The outstandings of this department have doubled over the past two years.

One way in which the Bank practices its specialty of "money mobilization" is through the Transcontinental Banking Service. This combines a modern communication system, pickup and delivery service from and to New York's airports, post office lock-boxes for mail collection and rapid processing of customer remittances, expense reimbursement plans for salesmen in the field, and procedures for prompt collection of freight charges. Through this service we are able to help customers keep their money effectively at work.

Although the pace has slowed from 1965, the Bank continues to be active in all phases of the mortgage business, including interim financing for construction and mortgage warehousing and long-term financing of business and residential properties. We are especially active in mortgage

loans to home buyers in the New York area. The Mortgage & Real Estate Loan Department is staffed by skilled personnel experienced in serving the complex needs of all segments of the mortgage market.

Specialists in Personal Services

Citibank has long been a leader in serving the financial needs of individuals. The Personal Finance Department, established 38 years ago, offers a wide variety of consumer credit services. Since its inception, the department has made 12,700,000 individual loans totaling $8.3 billion and currently has $540 million outstanding to 590,000 borrowers.

Over the past five years, Citibank has made loans for educational purposes totaling almost $100 million. This includes $60 million of loans made under New York State's low cost tuition loan program. We also offer a variety of our own financing plans to students who do not qualify for the New York State program.

In 1966, we introduced to the New York market a new service called "Checking Plus" which consists of an individual checking account plus a line of credit which the customer can utilize simply by writing checks. This service has proven to be effective both in attracting deposits and in generating additional loan income.

In December we announced the "Golden Passbook Account." This is a 90-day time deposit account paying 5% interest and utilizing a passbook record for the depositor's convenience. The minimum deposit is $1,000 and there is no maximum. The initial response has been gratifying and we hope to attract many new accounts.

Our services for travelers continue to grow. Sales of Citibank Travelers Checks again rose substantially. The number of on-the-spot refund and sales agencies has increased by 80% since 1960 and now exceeds 24,000 throughout the world.

Eight Travel Selection Centers, which bring both travel and banking services under one roof, were opened in New York during the year. We secure reservations for all types of transportation and accommodation. For clients going overseas we also provide letters of introduction and travelers' letters of credit.

Carte Blanche Corporation, in which we have a 50% interest, has moved to meet what has been a virtual explosion of competition in the credit card field from both new and established sources. Carte Blanche has increased both its total number of employees and its advertising and promotional budget in an effort to meet competition from sources such as oil companies, airlines, and groups of banks.

In 1966 the Carte Blanche Bankers Club franchise plan was inaugurated making it possible for a local bank to offer its own travel and entertainment credit card which will be honored by Carte Blanche associate establishments throughout the world. Another 1966 innovation permits cardholders to cash checks at any of our worldwide offices.

Science Fantasy Becomes Reality. *Citibank's public utilities experts assist electric companies in developing financing programs for the construction of facilities such as this giant atomic reactor at Oyster Creek, New Jersey. They also counsel public utilities managements on the development of individual long-term financing programs.*

We are continuing to establish new offices where they are needed in the New York metropolitan area. One of the 13 branches opened in 1966 is inside the new $40 million Hunts Point Market in the Bronx. It will serve the special banking needs of the fresh fruit and vegetable business located in the 126-acre market complex.

Money for Minicircuits. *Citibank's Aerospace and Electronics Department helps corporations in these wide-ranging fields to extend their know-how and production capacity to meet the nation's demand for technological leadership.*

New International Services

Citibank's specialists in international banking were active in 1966 in expanding the Bank's activities on all the six continents in which we operate.

Because of tight money conditions in Europe and our Government's measures restraining foreign investment by U.S. firms, our European branches have been making available short- and medium-term credit facilities in Eurodollars and certain other Eurocurrencies.

Last May our London City Office introduced the London dollar certificates of deposit. These are the Eurodollar counterpart of the negotiable certificates of deposit which we pioneered in New York in 1961. This new money market instrument has proven a useful addition to the short-term investment media available to holders of Eurodollars.

The Western Europe District has established a Correspondent Bank Department which provides correspondents in that area with the full range of Citibank's institutional facilities. Our network of European branches enables us to supply these banks and corporate customers with rapid collection service for foreign currency checks. European banks have responded with enthusiasm to new special procedures for speeding the collection of U.S. dollar checks at lower cost.

Corporate customers are always seeking ways to maximize their cash resources and have become expert in doing so domestically. This year we developed what we call Intercontinental Banking Service to enable multinational corporations operating in the United Kingdom and Western Europe to achieve closer control of their flow of international funds.

Expansion Abroad

With the opening of 18 new overseas offices in 1966, Citibank now has facilities in 60 countries and territories. Bolivia and the Virgin Islands were new areas added last year.

Each new branch extends the Bank's experience and knowledge in international banking to more and more customers. We recognize that a major commodity we have to offer our customers is professional counseling, not just money. Today, in many areas, Citibank officers combine the traditional roles of the commercial banker and the investment banker.

Through a subsidiary, International Banking Corporation, we acquired a 50% interest in the sales finance affiliate of Waltons Limited, one of Australia's leading retailers with 61 stores in New South Wales, Queensland, and Victoria.

Citibank has invested directly or through subsidiaries in a number of overseas financial institutions, including development banks in Ecuador, India, Liberia, Malaysia, Panama, Pakistan, the Philippines, and Venezuela. These private institutions, usually with strong local partners and government support, provide medium- and long-term funds for economic development in the private sector.

The services performed by overseas branches and affiliates differ considerably from country to country depending on local banking laws and traditions and the needs of various regions. Our offices range from a facility serving military personnel at Guantanamo Naval Base in Cuba to large, full-service branches in London, Rio de Janeiro, Tokyo, and other major cities. Increasingly we have been introducing U.S. retail banking services that are new to many countries.

Banking in Bolivia. *Citibank opened its branch in La Paz early in 1966. At year end, our offices in Central and South America totaled 69, including offices in every member nation of the Latin American Free Trade Association.*

Trust and Investment Specialists

In recent years, the spectrum of services offered by the Trust and Investment Division has been substantially broadened.

A major innovation in 1966 was the extension of our investment advisory service to customers who wish to invest $10,000 or more through the medium of a new Commingled Investment Account. The account operates without any entrance or withdrawal fees. Final approval to provide this service was received from the regulatory authorities last summer. The interest of customers has been encouraging and the number of participants continues to increase.

A new service for corporate customers results from the installation of Citibank's highly automated system for the processing and recording of participants' interests in profit sharing, thrift, and stock purchase plans. The service is designed to handle economically the great variety of mechanical and record-keeping needs of these plans.

Investment research personnel are also making important use of high-speed computers to process and evaluate a tremendous volume of statistics. Time-sharing computer facilities have been installed in the Investment Research Department and programs developed for using them.

In 1966, the varied trust and investment services offered to individual customers and their families were brought together in one administrative unit, Personal Investment Administration. As a result, an individual can now obtain through one Citibank officer any assistance he may require on any trust or investment matter. We thereby offer customers not only the in-depth skills and resources of the worldwide Citibank organization but also personal attention and administrative continuity.

Abroad, trust affiliates in the Bahamas, in England, and in Canada provide a variety of trust and investment services to U.S. individual and corporate customers operating overseas and to local individuals and businesses. These services are adapted to local laws, customs, and financial requirements and at the same time draw on the Bank's resources in New York, particularly investment research, trust experience, and operating knowledge.

Behind the Lines

All of the many services that our customer-oriented divisions offer would quickly come to a halt without the supporting activities of other divisions of the Bank.

Eighteen complete computer systems are kept in constant action by our Operating Division personnel. The division's Research and Development Department continually reviews and improves operating methods, work flows, and staff efficiency.

This department also prepares complex studies that often lead to the creation of new services which the Bank can offer, many of them on a fee basis. Typical of these is the new Broadscope Payroll Service which, in addition to performing all of a company's routine payroll operations, provides a wide range of information on labor costs, man-hours, and other related data.

Last year our Check Processing Department handled an average of 32 million checks a month—enough to reach from New York to California.

The Bank's Economics Department is a clearinghouse for a vast amount of economic data and business statistics from all over the world. The department holds regular briefings for senior officers and produces in-depth research reports as well as numerous publications, the best-known of which is the *Monthly Economic Letter*.

Our Bond Administration provides a broad range of money market services to corporate customers, correspondent banks, and the financial community. In making markets for all Treasury and Government agency issues, for state and local government securities, and for related short-term investments, our Bond Administration specialists help assure the mobility of funds that is essential to the efficient functioning of the nation's credit system. This was especially important under the stringent credit conditions that prevailed during most of 1966.

The Municipal Bond Department met the strains imposed by extraordinary activity in the secondary market for these securities. The volume of transactions handled was nearly double that of the preceding year.

Citibank has long held a leading position as an underwriter of municipal securities. However, the law makes no specific provision for banks to underwrite or deal in revenue bonds—issues of public bodies which are not general obligations but which are supported by the pledging of special tax receipts or the revenues of public projects. We naturally hope that Congress will see fit to rectify this. The competition of banks in this type of financing would enable public bodies to borrow at lower interest rates and would therefore seem to be clearly in the public interest.

Travelers' Aids. *Citibank operates this main branch and four satellite offices at Kennedy International Airport. The International Arrivals Branch is open around the clock to exchange currency, issue Travelers Checks, and cash checks for customers and Carte Blanche cardholders.*

Citibankers in Action

If the provision of financial services to meet customer needs is our primary mission, banking at First National City is nevertheless a far broader undertaking.

It is geographic—the many countries in which we offer our services. It is physical premises—the buildings, branches, and offices through which we provide our services. But most of all it is people, all kinds of people. More than 24,000 are employees. More than 67,700 are shareholders. Millions are customers who use one or more of our services.

Typically, when we announce a new service such as Checking Plus, or open a new branch or Travel Selection Center, or enter into an overseas affiliation, these activities are reported by the press and bring the name of First National City to the fore. But behind the news stories are the people of Citibank.

The goal of Citibankers is service. This and the following pages illustrate a few of the many people and their activities that contributed to this goal in 1966.

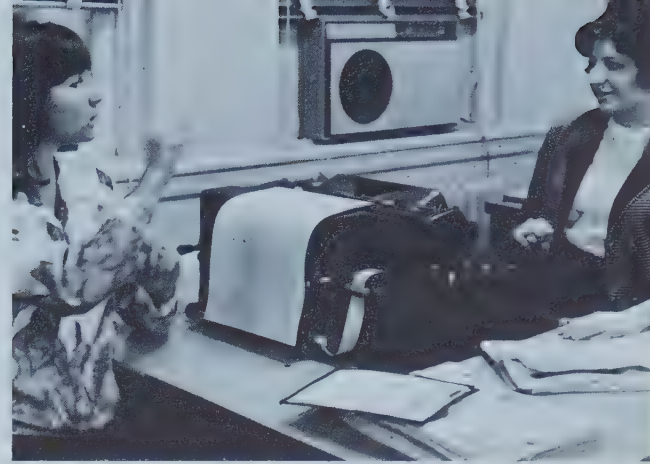
It is no exaggeration to say that the measure of our accomplishment in any year depends on the professional quality of Citibankers and the relationships they establish with the people on the other side of the desk or counter. From the officer who puts into practice the policies set by the Board of Directors to the teller who completes a transaction in a neighborhood branch, it is people who constitute Citibank and who give it character and vitality.

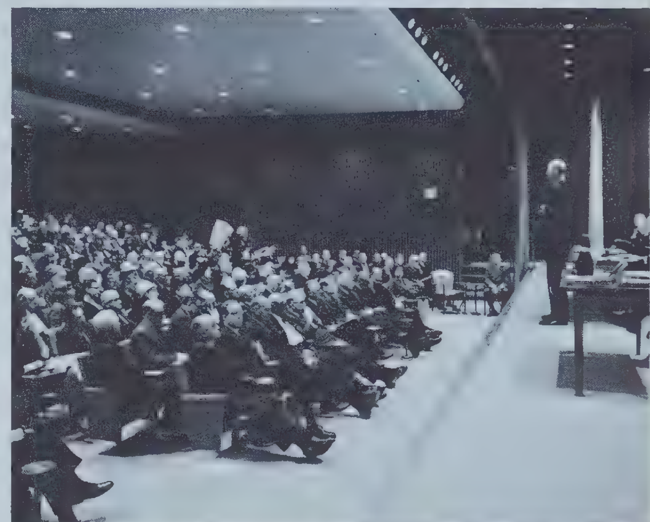
One evidence of the spirit of Citibankers is their enthusiastic response to staff new business campaigns. Last fall staff members throughout the metropolitan area participated in a sales incentive program that produced $223 million of new business, including $112 million in deposits.

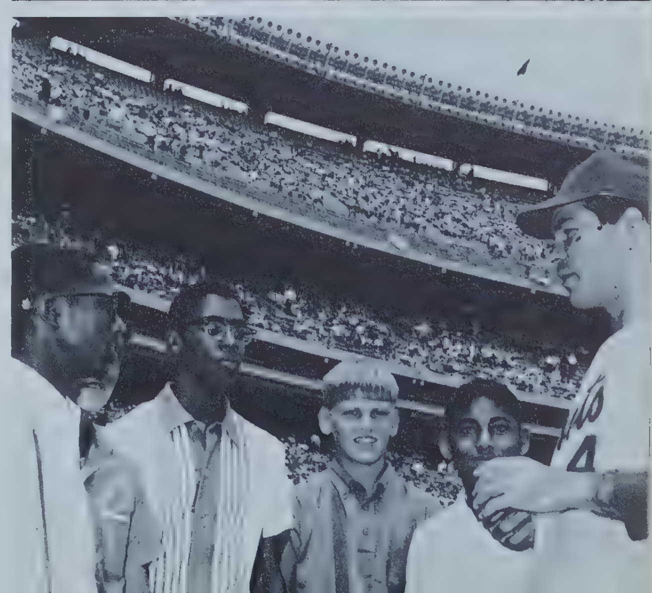
Citibankers in Training

Recognizing that a skilled, loyal staff is the cornerstone of success, the Bank places great emphasis on recruiting, training, internal communications, and supervisory relationships.

The search for talented individuals is never ending. In 1966 we interviewed more than 32,000 people to employ somewhat over 5,400. Representatives visited 75 college campuses and interviewed 1,500 students. In addition, selected high school graduates were recruited to enter special training courses designed for them.





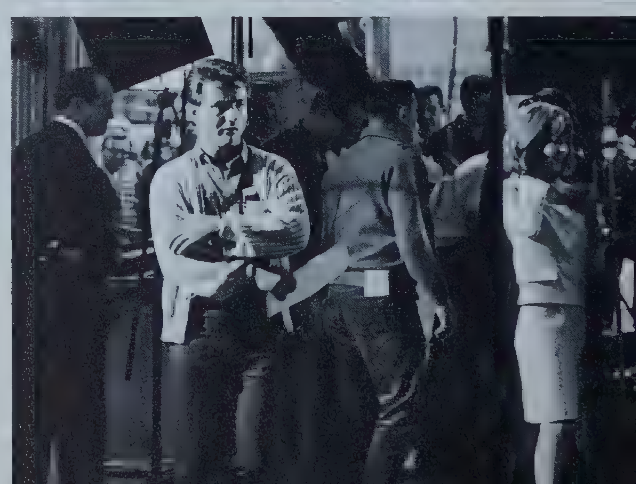


People Are Citibank. *Here, top to bottom: handicapped workers, hired under a new program, converse in sign language; Chairman James S. Rockefeller answers the questions of shareholders at the annual meeting; staff members sharpen skills with the latest teaching equipment, here with shortwave radio that provides prerecorded, individualized programmed instruction; a City Bank Club outing gives youngsters the opportunity to meet some of their heroes at Shea Stadium.*

The Bank also undertook programs to seek out qualified employees among the disadvantaged. These programs are especially successful and our efforts were recognized through the award of a Mobilization for Youth Certificate of Merit for "providing training and job opportunities for young men and women," and in a letter of commendation from the New York State Division of Vocational Rehabilitation for our employment of the handicapped.

We also expend great effort on training and development programs to assist Citibankers in improving their skills. In 1966, more than 7,800 employees participated in one or another of the Bank's programs. These include courses in our Training Center, tuition refunds for courses taken at local educational institutions, education and travel awards, and management development programs at universities.

As important as is the Bank's attitude toward its staff, even more important are the feelings of Citibankers about the Bank. During 1966, a survey was conducted for the Bank among all staff members in the metropolitan area. Many suggestions to improve service and efficiency, as well as helpful answers to management's questions, were provided

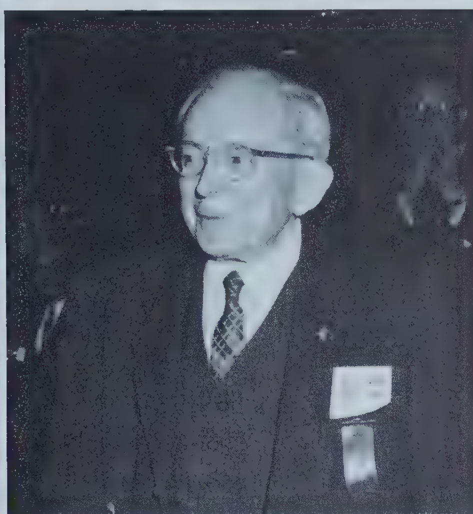


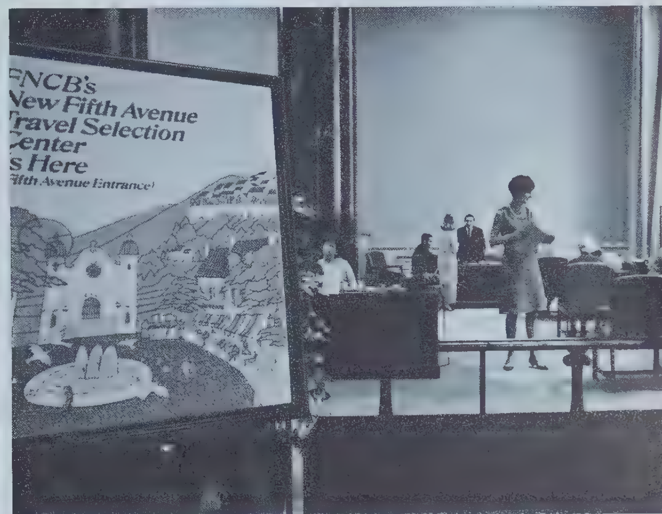
Citibank Is People: *The activities of Citibank and its affiliated organizations are carried out by thousands of people around the world. Pictured here, left to right,* (Top row): *a Citibank economist conducts a special course on New York City's economy for high school teachers; some of the members of the Bank's Policy Committee report on their respective divisions at a regular meeting of senior officers (L-R: Messrs. Pfeffer, Stott, Spencer, Cook, Bunnell, Wilcox, and Wriston); William M. Cockrell (left), president of Carte Blanche, and Willis J. Wheat, vice president of The Liberty National Bank and Trust Company of Oklahoma City, discuss the first participation in the Carte Blanche Bankers Club franchise plan.*

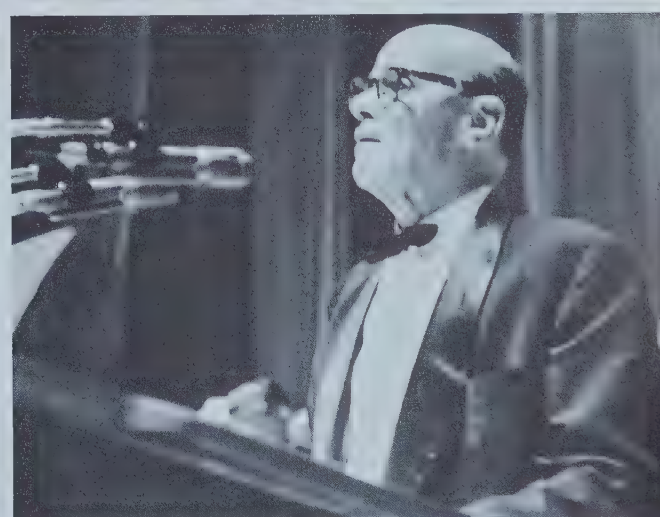
(Second row): *Personal loan officers counsel a young applicant on the Bank's student loan program; the Investment Research Library is the home for the annual reports of thousands of corporations as well as for other important financial data; William A. Duncan, former vice president, was the oldest member in attendance at the 30th annual banquet of the Citibank Quarter Century Club; eight Travel Selection Centers, including this one at our Fifth Avenue Branch, were opened in New York last year.*

(Third row): *Youngsters participating in Project Head Start get the feel of things on a visit to a metropolitan branch; through a subsidiary, the Bank acquired a 50% interest in the sales finance subsidiary of Waltons Limited in Australia; the Hubshman Factors Department, consolidated into the Bank in 1965, continues to expand its operations; George S. Moore, president, accepts 1966 Captain Robert Dollar Memorial Award from the National Foreign Trade Council honoring him and the Bank for their many contributions to advancing American foreign trade.*

(Bottom row): *One Saturday last spring, the 399 Park Avenue Headquarters was "on location" as a site for the filming of "Penelope"; three members of senior management, Messrs. Laeri, Palmer, and Hoguet, prepare for the Correspondent Bank Forum; with branches all around the world, the Overseas Division keeps track of the time on six continents; New York's massive transportation strike last January did not deter these Citibankers from making their way to work.*




FNCB's
New Fifth Avenue
ravel Selection
enter
s Here
Fifth Avenue Entrance)




WALTONS
TREADWAYS

by the respondents. The results of the survey are being reported to staff members and various constructive actions are being taken by management on the basis of the findings.

A second offering was made to employees eligible under our 1964 Stock Purchase Plan. Approximately 4,500 staff members participated.

Community Participation

Citibankers as individuals, as well as the Bank as an institution, have been active in many community programs. The City Bank Club, an employee organization, sponsored its annual orphans outing in the summer. At Christmas-time the Club gave 2,780 dolls and other gifts to children at local hospitals. During the year a total of $49,000 was contributed by staff members to the Greater New York Fund. More than 93% of all staff members in New York participated.

The Bank sponsored a voluntary course on "Economics for the Thinking Citizen" for staff members, distributed periodic reports on current issues to those who asked to receive them, invited prominent public officials to speak at staff public affairs forums, and provided teaching personnel and premises for a course on "Economics of New York City" for teachers in local high schools.

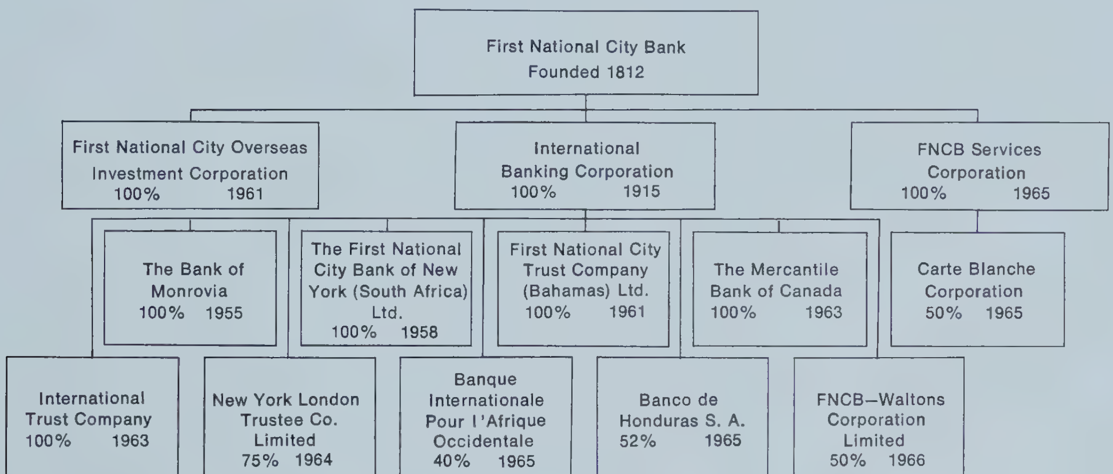
Recently the Bank published a report entitled "Metropolis New York," an analysis of the economy of the New York metropolitan area. Copies are available on request.

Another form of community participation involves the financial support of worthy causes by the Bank and the First National City Educational and Charitable Foundation. This past year $306,900 was distributed among 167 colleges and other educational institutions under our established plan of aid to higher education, and contributions totaling $723,600 were distributed among civic, charitable, health, and other organizations.

Last January, the sense of responsibility of Citibank people was dramatically demonstrated by their outstanding performance during the 12-day New York transit strike. Staff members who could not use Citibank's emergency bus transportation service walked, hitchhiked, bicycled, or even used roller skates to get to work. For many, the round trip took five hours or more. As a result of this devotion to banking service, all branches were kept open and operations were continued with a minimum of disruption.

Affiliated Companies

Laws and regulations of the United States and statutes of certain other nations require us to conduct some business through separate companies of which we own part or all of the stock. Listed with each company is the date of original acquisition and percentage owned by First National City. Below are descriptions of the major activities of each company and the names of directors other than officials of First National City.



First National City Overseas Investment Corporation is an Edge Act corporation which facilitates foreign capital transactions and makes equity investments abroad.

International Banking Corporation is a domestic company through which the Bank holds most of its interests in affiliates overseas.

FNCB Services Corporation enables the Bank to offer special types of services related to commercial banking.

The Bank of Monrovia conducts a general banking business and operates five offices in Liberia. Outside director: Henry Harfield.

The First National City Bank of New York (South Africa) Ltd. conducts a banking business and operates five offices in South Africa. Outside directors: D. D. Forsyth, H. L. Kennedy, E. B. Pagden, L. C. M. Rattray, and C. C. Wiley.

First National City Trust Company (Bahamas) Ltd. conducts a general trust business under the laws of the Bahamas and affords various legal and fiscal advantages to foreign customers and foreign subsidiaries of U.S. corporations. Outside directors: L. A. Astley-Bell, M. P. Maura, Col. A. T. Maxwell, Rt. Hon. Lord Rootes, Hon. Sir R. T. Symonette, and J. W. Walker, Q. C.

The Mercantile Bank of Canada conducts a general banking business and operates seven offices in Canada. Outside directors: A. Bachand, H. A. Benham, J. L. Black, W. J. Borrie, P. Côté, R. F. Elliott, Q. C., Hon. L. P. Gélinas, H. T. Mitchell, K. B. Palmer, O. B. E., Q. C., D. C. L., E. H. Tanner, O. B. E., and Maj. Gen. A. E. Walford, C. B., C. B. E., M. M.

Carte Blanche Corporation operates the Carte Blanche credit card business. Outside directors: L. W. Adams, W. M. Cockrell, H. Harfield, W. B. Hilton, C. W. Petersmeyer, and S. R. Zax.

International Trust Company conducts a general trust business and operates two offices in Canada. Outside directors: J. P. S. Mackenzie, F. Mercier, Q. C., and W. S. Robertson, D. F. C., Q. C.

New York London Trustee Co. Limited provides trust and investment services to companies in the United Kingdom. Outside directors: Viscount Bearsted, T. D., D. L., and Mr. G. H. Ross Goobey, F. I. A., F. S. S., S. I. S.

Banque Internationale pour l'Afrique Occidentale conducts a general banking business and operates 38 offices in central and western Africa. It also operates three offices in France. Outside directors: H. Bizot, A. de Boissieu, G. Froment-Meurice, H. S. Gerry, R. Klehe, R. M. O'Neill, J. Pallier, W. A. Prendergast, and P. Roques.

Banco de Honduras S.A. conducts a general banking business and operates six offices in Honduras. Outside director: A. S. Midence.

FNCB-Waltons Corporation Ltd. is a leading finance company in Australia with offices in Sydney, Brisbane, and Melbourne. Outside directors: L. Kingston, S. H. Proudford, A. E. Vrisakis, J. R. Walton, and J. S. Walton.

★ Uptown Headquarters, 399 Park Avenue, New York
☆ Downtown Headquarters, 55 Wall Street, New York
○ Offices Opened in 1966
WESTCHESTER
BRONX
MANHATTAN
QUEENS
NASSAU
BROOKLYN
RICHMOND

164 Offices in the Metropolitan Area

Uptown Headquarters, 399 Park Avenue, New York
Downtown Headquarters, 55 Wall Street, New York

Manhattan downtown
55 Wall Street
2 Broadway at Beaver St.
195 Broadway at Dey St.
107 William St. at John St.
125 Maiden Lane at Water St.
250 Broadway at Murray St.
Hudson St. at Franklin St.
Canal St. at Broadway
Grand St. at Bowery
160 Varick St. at Vandam St.
555 West Broadway
686 Broadway nr. Great Jones St.
72 Fifth Ave. at 13th St.
10 Irving Pl. nr. 14th St.
262 First Ave. opp. 15th St.
111 Eighth Ave. bet. 15th and 16th Sts.
*58 Duane St. at Elk St.
*411 Grand St. at Clinton St.

Manhattan midtown
399 Park Ave. at 53rd St.
141 E. 23rd St. nr. Lexington Ave.
Ave. of the Americas at 23rd St.
250 Fifth Ave. at 28th St.
1 Park Ave. at 32nd St.
Second Ave. at 32nd St.
Hubshman Factors, 90 Park Ave.
34th St. at Seventh Ave.
Fifth Ave. at 37th St.
Broadway at 40th St.
Second Ave. at 42nd St.
Lexington Ave. at 42nd St.
Madison Ave. at 42nd St.
448 W. 42nd St.
Vanderbilt Ave. at 44th St., Pan American Bldg.
Third Ave. at 46th St.
Park Ave. at 46th St.
640 Fifth Ave. at 51st St.
Ave. of the Americas at 52nd St.
Broadway at 56th St.
57th St. at First Ave.
Park Ave. at 57th St.
Ave. of the Americas at 57th St.

Manhattan uptown
Third Ave. at 63rd St.
Madison Ave. at 65th St.
162 Amsterdam Ave. at 67th St., Lincoln Square
First Ave. at 69th St.
72nd St. at Broadway
72nd St. at Third Ave.
Madison Ave. at 76th St.
First Ave. at 79th St.
123 E. 86th St. nr. Lexington Ave.
86th St. at Broadway
91st St. at Madison Ave.
96th St. at Broadway
111th St. at Broadway
116th St. at First Ave.
125th St. at Old Broadway
4249 Broadway nr. 181st St.
4949 Broadway nr. 207th St.

Queens
Bridge Plaza North at 29th St., Long Island City
Queens Blvd. at 39th St., Long Island City
Jackson Ave. at 46th Ave., Long Island City
Metropolitan Ave. at Flushing Ave., Maspeth
Thirtieth Ave. at 37th St., Astoria
22-16 31st St. nr. Ditmars Blvd., Astoria
51-31 Northern Blvd. nr. 51st St., Woodside
Roosevelt Ave. at 81st St., Jackson Heights
95-12 63rd Rd. nr. Queens Blvd., Rego Park
Continental Ave. at Austin St., Forest Hills
39-10 Main St., Flushing
70-78 Kissena Blvd., Flushing
25-47 Parsons Blvd. nr. Willets Point Blvd., N. Flushing
Francis Lewis Blvd. at 35th Ave., Bayside-Auburndale
Utopia Pkway. at Union Tpke., Fresh Meadows
89-50 164th St. nr. Jamaica Ave., Jamaica
John F. Kennedy International Airport Branches:
- Cargo Area
- First National City Bank Building
- International Arrivals Building
- Pan American Terminal
- TWA Terminal

Jamaica Ave. at 218th St., Queens Village
Union Tpke. at Lakeville Rd., Glen Oaks
*87-11 Queens Blvd. at 55th Ave., Elmhurst
*169-21 137th Ave. nr. New York Blvd., Rochdale Village
*61-03 Springfield Blvd., Oakland Gardens

Brooklyn
181 Montague St., Brooklyn Heights
370 Jay St. at Willoughby St., Brooklyn Heights
Livingston St. at Hanover Pl., Brooklyn Heights
Union St. at Columbia St., South Brooklyn
Clinton Ave. at Myrtle Ave., Fort Greene Park
Flatbush Ave. nr. Bergen St., Prospect
Nostrand Ave. at Herkimer St., Bedford-Stuyvesant
Myrtle Ave. at Bleecker St., Ridgewood
Manhattan Ave. at Noble St., Greenpoint
Pennsylvania Ave. at Liberty Ave., Brownsville
Flatbush Ave. at Church Ave., Flatbush
Kings Highway at E. 15th St., Kings Highway
3830 Nostrand Ave. at Ave. Z, Sheepshead Bay
Third Ave. at 35th St., Bush Terminal
Brooklyn Army Terminal†
Fifth Ave. at 54th St., Sunset Park
Thirteenth Ave. at 55th St., Borough Park
Fourth Ave. nr. 86th St., Bay Ridge
Eighteenth Ave. at 64th St., Bensonhurst
702 Utica Ave. nr. Clarkson Ave.

Richmond
1910 Victory Blvd., Castleton Corners
1495 Forest Ave., Port Richmond
2940 Richmond Terrace, Mariners Harbor
2595 Hylan Blvd., New Dorp
181 Richmond Ave., Port Richmond
577 Bay St. at Cross St., Stapleton
2825 Richmond Ave., Mid-Island
5810 Amboy Rd., Prince's Bay
1492 Hylan Blvd., Grasmere

Bronx
149th St. at Courtlandt Ave., North New York
505 Southern Blvd. nr. 149th St., St. Mary's Park
550 Hunts Point Ave. nr. Randall Ave., Hunts Point
1265 Castle Hill Ave., Castle Hill
1498 Metropolitan Ave., Parkchester
2481 Creston Ave. nr. Fordham Rd., Fordham
Kingsbridge Veterans Hospital†
5671 Riverdale Ave. nr. 259th St., Riverdale
1855 Bruckner Blvd. at Leland Ave.
1717 University Ave. nr. Tremont Ave., Morris Hts.
704 Allerton Ave. nr. White Plains Rd.
*2176 White Plains Rd. nr. Pelham Pkway., Lydig
*5660 Broadway nr. 233rd St., Kingsbridge
*3399 Boston Rd. at Wilson Ave., Hillside
*Hunts Point Market

Nassau
1316 Broadway, Hewlett
311 Sunrise Highway, Rockville Centre
1000 Old Country Rd. West of Ellison Ave., Garden City East
1000 Willis Ave. at I. U. Willets Rd., Albertson
960 Port Washington Blvd., Port Washington
180 West Merrick Rd., Freeport
2111 Merrick Ave. at Smith St., Merrick
1060 Hempstead Tpke. at Lexington Ave., Franklin Square
80 Jericho Tpke. at Brush Hollow Rd., Jericho
177 Jericho Tpke., Syosset
1125 Old Country Rd. nr. Plainview Rd., Plainview
250 Conklin St., Farmingdale
2940 Hempstead Tpke., Levittown
4881 Merrick Rd. nr. Park Blvd., Massapequa Park
3295 Sunrise Highway, Wantagh
*1110 Northern Blvd. nr. Community Dr., Manhasset
*2301 Jericho Tpke. at Nassau Blvd., Garden City Park

Westchester
95 Pondfield Rd., Bronxville
725 White Plains Rd. at Swift Ave., Eastchester
65 Main St. nr. Broadway, Hastings-on-Hudson
711 E. Boston Post Rd., nr. Barry Ave., Mamaroneck
825 Central Ave. nr. Ardsley Rd., Greenburgh
1040 Boston Post Rd. at Milton Rd., Rye
155 North Main St., Port Chester
92 North Broadway nr. McKeel Ave., Tarrytown
416 E. Sandford Blvd., Mt. Vernon
32 South Fifth Ave., Mt. Vernon
Main St. at Whippoorwill Rd., Armonk
66 South Moger Ave., Mt. Kisco
2004 Crompond Rd., Yorktown Heights
3000 E. Main St. (Rt. 6), Peekskill East
220 Westchester Ave. nr. Anderson Hill Rd., Harrison
37 Main St. at Hillside Ave., Elmsford
1920 Palmer Ave. nr. Chatsworth Ave., Larchmont
*895 Pelham Pkway. at Boston Post Rd., Pelham Manor
*51 Maple St. nr. Rt. 9, Croton-on-Hudson

†*Limited Banking Facility*
**Opened in 1966*

Metropolitan Regional Boards†

Nassau

Henry R. Bang
Assistant Vice President,
New York Telephone Co.

Ford Bartlett
President,
Lockwood, Kessler & Bartlett, Inc.

Dr. Arthur W. Brown
President,
Adelphi University

Martin Dwyer, Jr.
Sprague, Dwyer, Aspland & Tobin

T. John Folks, Jr.
Executive Officer &
Chairman of the Board,
Nassau Suffolk Lumber & Supply Corp.

Edgar S. Hill
Vice President,
Fairchild Camera & Instrument Corp.

Edward C. Nezbeda
Vice President,
Grumman Aircraft Engineering Corp.

Alexander Paulsen
General Apartments Corp.

Joseph Ushkow
President,
Endo Laboratories, Inc.

Howard B. Wakeman
Senior Vice President,
Long Island Lighting Co.

Staten Island

Andrew G. Clauson, Jr.
Chairman of the Board,
Sika Chemical Corp.

William A. Dreyer
President,
Arthur Dreyer & Son

Herbert A. Flamm
President
Weitzman's Photo Shop, Inc.

Arthur J. Grymes, III
Chairman of the Board & President,
Brewer Dry Dock Co.

Winston E. Himsworth
Vice President–Staten Island Operations,
The Brooklyn Union Gas Co.

Kenneth W. Nelson
President,
Tech Products, Inc.

William G. Quinn
Port Ivory Division Manager,
The Procter & Gamble Manufacturing Co.

Cornelius Vanderbilt
President,
Vanbro Construction Corp.

Walter L. Van Nostrand
Retired

Joseph Weissglass
President,
Weissglass Gold Seal Dairy Corp.

Westchester

David M. Brush
Treasurer,
General Foods Corp.

William N. Creasy
President,
Burroughs Wellcome & Co. (USA) Inc.

Bernard F. Curry, Jr.
President,
The Curry Corporation

George E. Heddy, Jr.
General Manager
New York Telephone Co.

T. Vincent Learson
President,
International Business Machines Corp.

Thomas D. Nast
President & Treasurer,
All-State Welding Alloys Co., Inc.

H. Halsted Park, Jr.
President,
H. H. Park, Inc.

M. Cabell Woodward, Jr.
Vice President–Finance
Continental Baking Co., Inc.

†*Other than members who are First National City Bank officials*


Canada
Montreal (2 branches)
Calgary
Halifax
Quebec
Toronto (2 branches)
Vancouver
Winnipeg
Mexico
Mexico City (5 branches)
Honduras
Tegucigalpa (2 branches)
Choluteca
Comayaguela (2 branches)
San Pedro Sula
El Salvador
San Salvador
Panama
Panama (5 branches)
Colon
Canal Zone
Balboa
Colombia
Bogota (2 branches)
Barranquilla
Cali
Cartagena
Medellin
Ecuador
Quito (2 branches)
Guayaquil
Peru
Lima (2 branches)
Callao
Bolivia
La Paz
Chile
Santiago (5 branches)
Concepcion
Valparaiso (2 branches)
Bahamas
Nassau (2 branches)
Guantanamo Bay
Jamaica
Kingston
Dominican Rep.
Santo Domingo (2 branches)
Puerto Rico
San Juan (5 branches)
Arecibo
Bayamon
Caguas
Mayaguez (2 branches)
Ponce
Virgin Islands
St Croix
Trinidad and Tobago
Port-of-Spain
Venezuela
Caracas (2 branches)
Maracaibo
Valencia
Brazil
Rio de Janeiro
Belo Horizonte
Brasilia
Campinas
Curitiba
Porto Alegre
Recife (Pernambuco)
Salvador (Bahia)
Santos
Sao Paulo (2 branches)
Paraguay
Asuncion (2 branches)
Uruguay
Montevideo (2 branches)
Argentina
Buenos Aires (6 branches)
Cordoba
Lomas de Zamora
Mendoza
Rosario
Germany
Berlin
Frankfurt
Hamburg
Netherlands
Amsterdam
Belgium
Brussels
Antwerp
England
London (2 branches)
Ireland
Dublin
France
Paris (2 branches)
Bordeaux
Marseilles
Switzerland
Geneva
Zurich
Italy
Milan
Mauritania, Islamic Rep. of
Nouakchott
Port-Etienne
Mali
Bamako
Senegal
Dakar (2 branches)
Kaolack
Ziguinchor
Upper Volta
Ouagadougou
Bobo-Dioulasso
Ivory Coast
Abidjan (5 branches)
Bouake
Liberia
Monrovia
Bomi Hills
Buchanan
Harbel
Nimba
Niger
Niamey
Magaria
Maradi
Zinder
Togo
Lome
Dahomey
Cotonou
Nigeria
Lagos
Apapa
Kano
Port Harcourt
Cameroon
Yaounde
Douala
Ebolowa
Garoua
Gabon
Libreville
Lambarene
Mouila
Port-Gentil
Branches
Subsidiaries
Affiliates
Representative Office
Military Facility

Fully-Staffed Offices Around the World

Consolidated Statement of Condition

Assets

	December 31, 1966	December 31, 1965
Cash and Due from Banks	$ 3,003,663,000	$ 2,463,795,000
U.S. Government Obligations	1,210,558,000	1,388,074,000
State and Municipal Securities	1,010,143,000	1,078,158,000
Other Securities	336,973,000	259,215,000
Loans, *after deducting Reserve for Possible Losses: 1966, $199,337,000; 1965, $183,056,000*	8,785,366,000	8,143,216,000
Customers' Acceptance Liability	262,763,000	267,588,000
Bank Premises and Equipment	145,983,000	142,076,000
Other Assets	310,098,000	234,665,000
Total	$15,065,547,000	$13,976,787,000

Liabilities

	December 31, 1966	December 31, 1965
Demand Deposits in Domestic Offices	$ 6,068,868,000	$ 5,616,854,000
Time Deposits in Domestic Offices	3,922,056,000	3,941,931,000
Deposits in Overseas Offices	2,948,676,000	2,390,099,000
Total Deposits	$12,939,600,000	$11,948,884,000
Acceptances Outstanding	268,518,000	274,984,000
Funds Borrowed	276,797,000	172,808,000
Accrued Taxes and Other Expenses	122,150,000	98,024,000
Provision for Dividend Declared	11,992,000	10,656,000
Other Liabilities	68,380,000	127,387,000
Unearned Income	71,127,000	74,311,000
Reserve for Contingencies	117,500,000	106,613,000

Capital Accounts

	1966	1966	1965	1965
4% Convertible Capital Notes Due 1990	$266,308,000		$266,308,000	
Capital Stock ($13.50 par) 26,648,871 shares in 1966; 26,639,838 in 1965	$359,760,000		$359,638,000	
Surplus	401,285,000		400,943,000	
Undivided Profits	162,130,000		136,231,000	
	$923,175,000	1,189,483,000	$896,812,000	1,163,120,000
Total		$15,065,547,000		$13,976,787,000

Explanatory notes are on pages 30-31.

Consolidated Statement of Earnings

	1966	1965	Change
Operating Income			
Interest on Loans	$391,288,000	$326,782,000	$+64,506,000
Interest and Dividends on Securities			
—U.S. Government	50,238,000	49,996,000	+ 242,000
—State and Municipal	37,914,000	35,200,000	+ 2,714,000
—Other Securities	6,224,000	5,065,000	+ 1,159,000
Other Income	85,798,000	69,402,000	+16,396,000
	$571,462,000	$486,445,000	$+85,017,000
Operating Expenses			
Provision for Staff Payments			
—Salaries	$ 96,579,000	$ 87,674,000	$+ 8,905,000
—Profit Sharing	5,623,000	4,940,000	+ 683,000
—Retirement and Group Insurance	11,214,000	10,682,000	+ 532,000
—Social Security Taxes	4,111,000	3,268,000	+ 843,000
—Hospitalization and Medical	1,004,000	1,063,000	— 59,000
	$118,531,000	$107,627,000	$+10,904,000
Interest	233,510,000	184,837,000	+48,673,000
Deposit Insurance Assessment	3,073,000	3,076,000	— 3,000
Premises *(net)*	20,745,000	19,414,000	+ 1,331,000
Other Expenses	45,205,000	40,512,000	+ 4,693,000
	$421,064,000	$355,466,000	$+65,598,000
Net Before Income Taxes	$150,398,000	$130,979,000	$+19,419,000
Taxes Based on Operating Income	45,508,000	37,250,000	+ 8,258,000
NET OPERATING EARNINGS	$104,890,000	$ 93,729,000	$+11,161,000
Per Share	$3.94	$3.52	$+.42
Net Profit or *Loss* from Sales of Securities*	$ *5,432,000*	$ 380,000	
Provision for Loan Losses* (Equal to Net Charge-offs against Reserve for Possible Losses On Loans)	*6,055,000*	*5,441,000*	
Transferred to Undivided Profits	$ 93,403,000	$ 88,668,000	

Changes in Consolidated Capital Accounts

	1966	1965
Balance at Beginning of Year	$1,163,120,000	$ 874,305,000
Additions		
Transferred to Undivided Profits	$ 93,403,000	$ 88,668,000
Sale of 4% Convertible Capital Notes Due 1990	—	266,308,000
Sale of Stock Under Staff Option and Purchase Plans	464,000	1,148,000
Other Additions	80,000	4,000
	$ 93,947,000	$ 356,128,000
Deductions		
Provision for Cash Dividends	$ 46,629,000	$ 42,614,000
Transferred to:		
Reserve for Possible Losses On Loans*	8,482,000	12,506,000
Reserve for Contingencies	12,294,000	12,039,000
Other Deductions	179,000	154,000
	$ 67,584,000	$ 67,313,000
Balance at End of Year	$1,189,483,000	$1,163,120,000

*After tax provision

Explanatory notes are on pages 30-31.

Notes to the Financial Statements

Note 1: Basis of Presentation

The Consolidated Statement of Condition includes the assets and liabilities of the Bank and its wholly-owned subsidiaries. For comparability, 1965 figures for the provision for loan losses have been reclassified to conform with the 1966 treatment.

Figures of overseas offices are as of December 20, and are converted at rates of exchange current on that date. Earnings of overseas offices are included in Other Income in the Consolidated Statement of Earnings only if the earnings are remittable to the United States.

Note 2: Assets

Investment securities are carried at cost less amortization of premiums. At December 31, 1966, the market value of the securities portfolio is approximately $60,000,000 below the book value of $2,557,674,000.

Bank premises and equipment are carried at cost less accumulated depreciation. The expenses in 1966 include $8,126,000 for depreciation, and $8,829,000 for rental cost of leased premises and equipment, generally at terms not in excess of thirty years. The Bank has entered into lease obligations for certain premises not yet occupied, which when occupied will increase annual rentals by approximately $4,300,000.

U.S. Government obligations carried at $650,896,000, State and Municipal securities carried at $427,620,000 and other assets carried at $167,228,000 on December 31, 1966 are pledged to secure public and trust deposits and for other purposes.

Note 3: Retirement Plans

Each year the Bank pays to the Trustee an amount sufficient to provide for current service benefits under the Retirement Plan and to continue the program of funding past service benefits. The remaining liability of approximately $5,500,000 with respect to past service is expected to be fully funded by 1969.

The Group Insurance Plan continues protection on a reduced basis at the Bank's expense for staff members after they retire. At the end of 1966, estimated future death benefits on the lives of present pensioners amount to approximately $22,000,000. Premiums paid to the insurance company include the current cost of these benefits.

Note 4: Convertible Capital Notes

The 4% Convertible Capital Notes Due 1990 are convertible into Capital Stock at a conversion price of $66⅔ per share, subject to adjustment in certain events. The Notes, which are subordinated to obligations to depositors and other creditors, are redeemable on or after July 1, 1970 at the option of the Bank, in whole or in part, at their principal amount plus accrued interest and a premium initially of 3.05%, declining thereafter, and without premium on or after July 1, 1986. Interest on the Notes in 1966 of $10,652,000 is included in Interest expense.

Note 5: Capital Stock

Of an authorized 35,000,000 shares at December 31, 1966, 5,967,722 are reserved for issuance in connection with conversion of the Capital Notes and sales under the Stock Option and Purchase Plans described below.

The Capital Notes indenture prohibits the payment of dividends (other than stock dividends) or the purchase of outstanding Capital Stock in amounts which would reduce the total of the Capital, Surplus, and Undivided Profits below $800,000,000.

Under the Bank's Stock Option Plan for key personnel, as of December 31, 1966, 40,479 shares of Capital Stock have been purchased (5,763 in 1966) and options for 892,807 shares with an aggregate option price of $46,759,314 remain outstanding. The options have been granted for terms up to 10 years at not less than the fair market value of the shares at the dates of grant, and are exercisable cumulatively in equal annual installments.

As of December 31, 1966, participants in the Stock Purchase Plan have purchased 6,412 shares of Capital Stock (3,270 in 1966) at the fair market value of the shares at the dates of grant, and rights to purchase prior to October 5, 1968 remain outstanding for an additional 72,950 shares at an aggregate purchase price of $3,674,856.

Note 6: Reserves

The Reserve for Possible Losses On Loans is a statutory reserve, the maximum amount of which is governed by Treasury Department regulations. Recognized loan losses are charged to this reserve and subsequent recoveries are added. This reserve has been deducted from Loans in the Consolidated Statement of Condition. Changes in this reserve and Reserve for Contingencies in 1966 are shown in the table below.

Changes in Consolidated Reserves		Reserve For Possible Losses On Loans	Reserve For Contingencies
Balance at December 31, 1965		$183,056,000	$106,613,000
Deductions			
Net Loan Charge-offs		$ 12,419,000	—
Other Deductions		—	$ 3,341,000
		$ 12,419,000	$ 3,341,000
Additions			
Per Treasury Department Regulations			
Due to Net Loan Charge-offs			
Transferred from Earnings	$6,055,000		
Tax Reduction	6,364,000	$ 12,419,000	—
Due to Increase in Loans			
Transferred from Undivided Profits	$8,482,000		
Tax Reduction	7,799,000	16,281,000	—
Transferred from Undivided Profits		—	$ 12,294,000
Other Additions		—	1,934,000
		$ 28,700,000	$ 14,228,000
Balance at December 31, 1966		$199,337,000	$117,500,000

Auditors' Report

PEAT, MARWICK, MITCHELL & CO.
CERTIFIED PUBLIC ACCOUNTANTS
SEVENTY PINE STREET
NEW YORK, NEW YORK 10005

The Board of Directors
First National City Bank:

We have examined the consolidated statement of condition of First National City Bank and wholly-owned subsidiaries as of December 31, 1966 and the related statements of earnings and changes in capital accounts for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated statement of condition, consolidated statement of earnings and changes in consolidated capital accounts present fairly the financial position of First National City Bank and wholly-owned subsidiaries at December 31, 1966 and the results of their operations and changes in capital accounts for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

January 17, 1967

Peat, Marwick, Mitchell & Co.

Ten Year Record

Year-end	Assets—In Millions: Total Assets	U.S. Government Obligations	State and Municipal Securities	Loans	Deposits—In Millions: In Domestic Offices: Demand	Time	In Overseas Offices	Total
1956	$ 7,588	$1,264	$ 411	$3,741	$5,154	$ 917	$ 722	$ 6,793
1957	7,803	1,236	413	3,870	5,074	904	839	6,817
1958	8,088	1,588	546	3,839	5,050	1,225	853	7,128
1959	8,298	1,108	462	4,420	5,211	1,062	962	7,235
1960	8,832	1,534	513	4,260	5,497	1,262	1,012	7,771
1961	9,646	1,885	700	4,403	5,786	1,576	1,100	8,462
1962	10,449	1,519	780	5,045	5,806	2,031	1,348	9,185
1963	11,798	1,307	970	6,119	6,012	2,745	1,668	10,425
1964	12,452	1,372	1,065	6,778	5,636	3,335	1,835	10,806
1965	13,977	1,388	1,078	8,143	5,617	3,942	2,390	11,949
1966	15,066	1,211	1,010	8,785	6,069	3,922	2,949	12,940

Year-end	Per Share*: Capital, Surplus, and Undivided Profits	Net Operating Earnings	Cash Dividends Declared	In Thousands: Shares Outstanding*	Shareholders	Staff
1956	$60.22	$5.20	$2.65	10,000	63,893	16,100
1957	61.31	5.02	2.95	12,000	71,460	16,800
1958	62.31	5.02	3.00	12,000	71,222	17,000
1959	63.76	5.66	3.00	12,000	69,663	17,900
1960	64.55	6.07	3.00	12,240	69,909	18,400
1961	64.80	5.84	3.00	12,485	68,857	19,500
1962	65.13	5.80	3.00	12,784	67,817	19,800
1963	65.25	5.90	3.00	13,040	67,487	20,700
1964	65.70	6.52	3.05	13,308	67,123	20,800
1965	33.66	3.52	1.60	26,640	67,793	22,100
1966	34.64	3.94	1.75	26,649	67,721	24,000

Year-end	In Thousands: Net Operating Earnings	In Millions: Capital Stock	Surplus	Undivided Profits	Total	Convertible Capital Notes	Total Capital Accounts
1956	$ 51,962	$210	$310	$ 82	$602		$ 602
1957	60,205	250	390	96	736		736
1958	60,274	250	390	108	748		748
1959	67,962	250	400	115	765		765
1960	74,292	255	390	145	790		790
1961	72,861	260	410	139	809		809
1962	74,108	256	420	157	833		833
1963	76,942	261	420	170	851		851
1964	86,794	266	421	187	874		874
1965	93,729	360	401	136	897	$266	1,163
1966	104,890	360	401	162	923	266	1,189

*2% stock dividends were paid 1960 through 1964 and a 2-for-1 stock split was effected in 1965.

Senior Management

Chairman
JAMES S. ROCKEFELLER

President
GEORGE S. MOORE

Chairman of the Executive Committee
RICHARD S. PERKINS

Vice Chairman
J. HOWARD LAERI

Executive Vice Presidents
A. HALSEY COOK
ROBERT L. HOGUET, JR.
EDWARD L. PALMER
WILLIAM I. SPENCER
THOMAS R. WILCOX
WALTER B. WRISTON

Chairman Credit Policy Committee
GEORGE C. SCOTT

Comptroller
BERNARD T. STOTT

Senior Vice President
DELMONT K. PFEFFER

Senior Vice President and Cashier
CARL W. DESCH

Senior Vice President and Economist
LEIF H. OLSEN

Senior Vice Presidents
E. SHERMAN ADAMS
CONRAD F. AHRENS
JOHN B. ARNOLD
GEORGE E. BARNETT, JR.
LELAND S. BROWN
H. LANSING CLUTE
E. PETER CORCORAN
G. A. COSTANZO
THOMAS F. CREAMER
E. NEWTON CUTLER, JR.
LOREN A. ERICKSON
JOHN EXTER
STEPHEN C. EYRE
ROBERT W. FEAGLES
JOHN F. FITZGERALD
LESTER GARVIN
HENRY M. HUBSHMAN, JR.
JAMES F. JAFFRAY
JULIEN-PIERRE KOSZUL
JOHN J. LARKIN
HOMER C. LATHROP
GEORGE M. LINGUA
WILLIAM A. LOCKWOOD
DONOLD K. LOURIE
P. HENRY MUELLER
EBEN W. PYNE
EDWIN A. REICHERS
JUAN D. SANCHEZ
JOHN C. SLAGLE
JOHN E. THILLY
HULBERT W. TRIPP
ALFRED M. VINTON

Deputy Comptroller
JOHN C. MACY

Budget Director
ROBERT V. OWEN

Vice Presidents
JAMES H. ALLEN
ALBERT W. AMBS
ROBERT D. ARNOLD
DAVID S. BAKER, JR.
WILBUR C. BALDWIN
J. WILLIAM BARGFREDE
ARTHUR R. BESEMER
CHARLES W. BISSET
WALTER BLENK
JOHN J. BLUMERS
JOSEPH J. BORGATTI, JR.
KENNETH A. BOTT
PATRICK F. BOWDITCH
FREDERICK W. BRADLEY, JR.
JAMES A. BRENNAN
T. CONWAY BREW
HUGH C. BREWER, JR.
J. EDMUND BULL
ROLLIN C. BUSH
EUGENE J. CALLAN
THOMAS F. CARROLL
DAVID S. CAULKINS
GEORGE J. CLARK, JR.
H. VAN B. CLEVELAND
THOMAS J. CLOUGH
CLARKE COGGESHALL
PAUL J. COLLINS
PHILIP CONWAY
BRIANT S. COOKMAN
WILLIAM F. CORDNER
WILLIAM M. CRANE
LOUIS D. CULLINGS
SIDNEY W. DAVIDSON, JR.
GEORGE L. DAVIS
JAMES S. DEELY
PETER DEL COL
DANIEL C. de MENOCAL
ROBERT W. DEUCHAR
ROY H. DICKERSON
DANIEL D. DICKEY
RICHARD B. DICKSON
JOHN T. DIMON
JOHN P. DOWD
HARRY G. DUNN
JOHN H. EARLY
GEORGE P. EGBERT, JR.
ANTHONY T. ELLIS
ROBERT S. EMISON
DONALD R. EVANS
JAMES D. FARLEY
WILFORD M. FARNSWORTH, JR.
DOUGLAS A. FIRMIN
WILLIAM W. FLANAGAN
JOSEPH H. FLEISS
RICHARD W. FREUND
JAMES G. GAFFNEY
E. THEODORE GARDNER
FREDERICK W. GILL
BERNARD F. GINNITY
WALTER GLESS
CHARLES C. GOODFELLOW
JOHN C. GOODRIDGE
ROBERT P. GRAHAM
ROBERT E. GRANT
GLEN K. GREEN
WILLIAM J. HARVEY, JR.
JOHN D. HASHAGEN
RODNEY N. HATCHER
WILLIAM T. HAYES
LAWRENCE S. HEATH, II
JOHN W. HEILSHORN
T. JACK HENRY
WILLIAM G. HERBSTER
PHILIP W. HESTON
B. DOUGLAS HILL
HERBERT HOLDEN, JR.
J. GARRARD HOLT
DAVID L. HOLZMAN
CLARENCE V. HORAN, JR.
MICHAEL J. HORGAN
DeWITT HORNOR
DONALD S. HOWARD
ALFRED H. HOWELL
J. REED HUMMER
FREEMAN H. HUNTINGTON
LAWRENCE W. HUSE
ROBERT L. HUSTON
JOHN W. INGRAHAM
WALTER W. JEFFERS
LEONARD F. JOY
RAYMUND A. KATHE
RICHARD F. KEZER
PAUL W. KIMZEY
PAUL H. KOLTERJAHN
CARL KRIECH
MIROSLAV A. KRIZ
CEDRIC R. LANE
NORMAN J. LARKIN
RICHARD L. LeKACHMAN
JOHN F. LENNON
SAMUEL LORD, JR.
WILLIAM T. LOVELAND
WILLIAM W. LOWE
HOWARD B. MacADAMS
ROBERT P. MacFADDEN
WILLIAM M. R. MAPEL
BERNARD J. MARTIN
JOHN M. MARTIN
FRANK de C. MATTHEWS
GERALD M. MAYER, JR.
JULIEN L. McCALL
JOSEPH J. McDERMOTT
FRANK A. McGLYNN
COLEMAN B. McGOVERN, JR.
DAN C. McNEILL
A. JAMES MEIGS
ARTHUR C. MERRILL
W. HOWARD MILLER
PAUL D. MILLHOLLAND
HAROLD M. MILLS
ARTHUR B. MITTWOCH
PATRICK J. MULHERN
HENRY J. MULLER
LEWIS C. MURDOCK
WILLIAM G. NAGLE
HERBERT E. NEVINS
PARKER E. NIELSEN
THOMAS H. O'BRIEN
PHILIP J. ORSI
WILLIAM E. PANITZ
ROBERT C. PARADISE
MICHAEL PESCATELLO
ALAN W. PETERS
JOHN E. PORTA
VICTOR O. PRALL
FRANCIS VERNON QUEEN
JAMES H. REDINGTON
CHARLES H. REEVES
JOHN J. REYNOLDS
WILLIAM F. REYNOLDS
ROBERT RICE
REUBEN F. RICHARDS
WALTER J. RIETHER
JUAN A. RIVERA
GEORGE H. ROBERTS, III
MALCOLM W. ROBINSON
CHRISTOPHER R. P. RODGERS
EMIL L. ROLLNICK
GENE ROMEI
JEREMIAH K. ROSS, JR.
WILLIAM A. ROUGH
JOHN RULON-MILLER
GEORGE P. RUTLAND, JR.
RAYMOND H. SAMPSON
FRANKLIN R. SAUL
H. ERIC SCHMIDT
M. H. SCHWARTZ
DAVID W. SCULLY
WALTER S. SEIDMAN
GERALD E. SHERROD
ROBERT D. SIFF
ROBERT B. SILLECK
ALBERT V. SILVA
KENNETH M. SPANG
JOHN P. STANTON
CHARLES O. STAPLEY
FRED A. STECHER
WARD B. STEVENSON
CARLETON M. STEWART
RODERIC B. SWENSON
RICHARD E. THOMAS
PETER A. TILESTON
FREDERICK J. TODD
STEPHEN VAN RENSSELAER
JOHN F. VAUZANGES
RICHARD S. VOKEY
MANNING W. VOORHEES
EDWARD WALDMAN
F. THOMAS WARD, JR.
PETER F. WAY
BASIL C. WEHRMAN
ALAN McK. WELTY
WARREN WHEELER
EDWARD B. WHITE
JOHN F. WINCH
JOHN G. WINSLOW
DOUGLAS F. WULFFLEFF
GEORGE YATES

Director of Education
and Training Research
DONALD W. DEVINE

Argentina		Australia		Bahamas		Belgium		Bolivia
	Brazil		Cameroon		Canada		Central African Rep.	
Chad		Chile		Rep. of China		Colombia		Congo Republic
	Dahomey		Dominican Republic		Ecuador		El Salvador	
France		Gabon		Germany		Greece		Honduras
	Hong Kong		India		Ireland		Italy	
		Ivory Coast		Jamaica		Japan		
				United States				

FIRST NATIONAL CITY BANK

Annual Report 1966

	Lebanon		Liberia		Malaysia		Mali	
Islamic Rep. of Mauritania		Mexico		Netherlands		Niger		Nigeria
	Pakistan		Panama		Paraguay		Peru	
Philippines		Puerto Rico		Saudi Arabia		Senegal		Singapore
	Rep. of South Africa		Switzerland		Togo		Trinidad & Tobago	
Dubai, Trucial States		United Kingdom		Upper Volta		Uruguay		Venezuela

Serving throughout the World. *These are the countries and territories in which Citibank has branches and affiliates and whose flags appear on the front cover. The colors and proportions of certain flags have been adjusted to achieve optimum reproduction.*

FIRST NATIONAL CITY BANK
399 Park Avenue
New York, N.Y. 10022

September 1966

AR41

Monthly Economic Letter

1812 FIRST NATIONAL CITY BANK NEW YORK 1966

General Business Conditions

Dramatic declines in stock prices and a continuing climb in interest rates dominated the news in an eventful August. As the Dow-Jones industrial stock average dropped 14 per cent between July 8 and August 29, businessmen and investors were torn between mounting concern over inflation and the squeeze of tight money. Against a background of rising consumer prices, inflationary worries were intensified by the guidepost-shattering 5 per cent wage increase won by the airline mechanics. Interest rates rose further and banks raised their prime lending rates, as the Federal Reserve withdrew a substantial amount of reserves from the banking system even as credit demands expanded.

On the surface it may be hard to see any substantial effects of the credit squeeze on the economy as a whole. Business news is full of glowing reports about record industrial production and rising order backlogs, new peaks in personal income, sustained consumer buying plans, and favorable corporate earnings. Even auto sales have been strong enough to pull dealer inventories down below where they were a year ago.

CONTENTS PAGE

General Business Conditions 97
The Squeeze on Housing • Tightening Credit Markets • Experiment in Credit Control • Money Supply Down

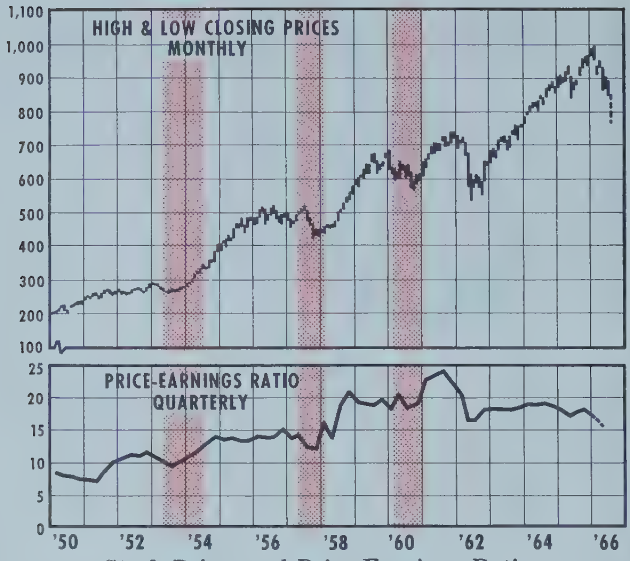
Prices, Guideposts and Anti-Inflation Policy . 100
A More Flexible Guidepost Policy • What the Price Indexes Show • Policy Lessons from 1956-57 • Is Demand Excessive? • Restricting Demand vs. Boosting Supply

World Trade Negotiations: A Progress Report 104
The Trade at Stake • The Pattern of Issues • The Need for Positive Results • Regionalism and Multilateralism

However, it is still early for the broad economic implications of monetary policy to become clearly visible. Certainly, bankers and borrowers alike are aware that credit policy is biting deeply into many areas of economic activity. One of the best publicized victims of the shortage of money is the stock market. With a wide array of investment opportunities bidding for money, holders of cash will buy stocks only at more attractive yields, i.e. lower prices. In the continuous exchange of cash for equities, they have become cheaper and cheaper. As paper values evaporate and some losses are actually realized, the earlier expansive sentiment of investors and businessmen is, of course, sharply altered. Earlier this year investors were concerned that a corporate tax increase might force stock prices lower. But tight money has pushed them down at least as far and possibly farther than could have been achieved by a tax hike. In fact, the stock market jumped sharply on August 31 when news of a possible increase in taxes was announced. Presumably the hope was that higher taxes would enable monetary authorities to ease up on credit policy.

The Squeeze on Housing

Another area hard hit by tight credit is housing. By July the number of private nonfarm dwellings started had dropped to a seasonally adjusted annual rate of 1,044,000, down 28 per cent from a year earlier and the lowest since December 1960. Builders of both single-family and multi-family housing have had difficulty



Stock Prices and Price-Earnings Ratios
Dow-Jones Industrial Average

getting commitments for construction loans and new home buyers find mortgages increasingly hard to obtain. The market for existing homes has been narrowed largely to cash buyers or those who can make substantial downpayments. This is slowing the transfer of homes from one owner to another, reducing real estate values.

In an attempt to ease the plight of the housing market, Congress enacted and sent to the President legislation to channel as much as $4.8 billion into the mortgage market through the Federal National Mortgage Association. In order to pour this money into the mortgage market, FNMA will have to dip most of it out of the capital market—both directly and through the Treasury. Raising fresh money on this scale in an already strained capital market will tend to raise interest rates there, but should relieve some of the anxieties that have affected the mortgage market.

Of course, not all the ills of the housing industry can be blamed on the scarcity of mortgage funds. Overbuilding earlier in the 1960's produced a hangover of high vacancy rates in some parts of the country—notably Southern California—that still persists. The U.S. Department of Commerce figures, shown in the accompanying table, document the decline in housing in the West which began nearly three years ago, while in the rest of the nation homebuilding remained strong until the second quarter of this year.

Tightening Credit Markets

The impact of credit demands and monetary policy on financial markets scarcely needs embellishment. Yields on new corporate bond issues advanced as the volume of offerings was heavy. As an indication of the increase in rates, the most recent Aa-rated utility issue was by the end of August priced in the market to yield 6⅛ per cent—about half of a percentage point higher than the yield on a similar issue a month earlier.

Treasury and municipal bonds also sold off sharply. Bond rates are generally a half to a full percentage point above their previous postwar peaks in late 1959 and early 1960. With the exception of 1920-21, moreover, bond yields are the highest in nearly a century.

Short-term rates have also been climbing. Yields on six-month Treasury bills have risen above 5¾ per cent, and commercial paper rates are 5⅝-5⅞ per cent. A one-year Treasury bill was auctioned last month at a 5.84 per cent discount rate—equivalent to a bond rate of 6.20 per cent—and one-year Federal agency issues can be purchased in the market at yields as high as 6¼ per cent. The minimum bank lending rate to business borrowers was raised by one quarter of a percentage point in response to money costs and to extraordinary loan demands.

Nonborrowed reserves—the reserves banks obtain as a result of Federal Reserve open market operations—declined $585 million in the four weeks ended August 24, compared with a decline of $144 million in the like period of 1965 and an increase of $136 million in 1964. As a result, the money supply—checking accounts and currency in circulation—which had declined persistently since late June, contracted further in August. Meanwhile, time deposits continued to grow at a markedly slower rate than in 1965. The ability of individuals and institutions to lend, spend and invest is being sharply curtailed.

Experiment in Credit Control

Recent statements and actions indicate that the monetary authorities are focusing much of their attention upon trying to slow down busi-

New Private Housing Starts

Year	Thousands of dwelling units: West*	Thousands of dwelling units: Rest of U.S.	Per cent change from year earlier: West*	Per cent change from year earlier: Rest of U.S.
1963	431	1,178	+14	+9
1964	365	1,193	−15	+1
1965	276	1,229	−24	+3
1966†	242	1,145	−17	−5

* Includes Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming.

†Seven months, seasonally adjusted annual rate.

Source: U.S. Department of Commerce.

ness investment spending through limiting expansion of bank loans to business. While attempting to dampen business investment is not a new tactic for a central bank which is fighting inflation, the effort this time involves some new techniques.

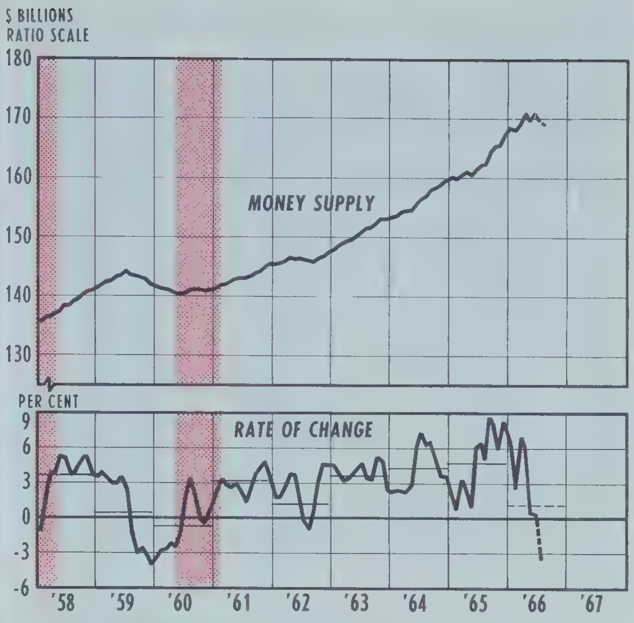
The main new technique consists of trying to reduce commercial bank issuance of negotiable certificates of deposit. Thus, the Federal Reserve Board announced that increases in reserve requirements on time deposits, from 4 to 6 per cent in two steps, were "designed to exert a tempering influence on bank issuance of time certificates of deposit, and to apply some additional restraint upon the expansion of bank credit to businesses and other borrowers." These increases—effective in July and September—raise the cost of time deposits by about ⅛ of a percentage point at large banks. Furthermore, the Regulation Q ceiling rate has been held at 5½ per cent in the face of rising market rates of interest. Under that limit it becomes difficult for banks to replace maturing CDs when rates on competing short-term Treasury bills and other instruments are well above 5½ per cent.

The selectivity of this new control technique stems from the fact that the larger banks, which tend to specialize in business lending, have depended upon certificates of deposit for much of their growth since 1961.

As a further refinement of the new control technique, the announcement of the most recent reserve requirement increase implied that banks losing funds from a runoff of time deposits will be able to resort temporarily to borrowing from the Federal Reserve Banks, until they are able to make adjustments in their portfolios. These adjustments are "expected to emphasize increased restraint in lending policies and maintenance of an appropriate degree of liquidity on the part of borrowing banks."

The contraction in member bank reserves (seasonally adjusted) since last April, the rise in loan-to-deposit ratios, growing pressures on bank liquidity, and higher loan rates have for some months been generating increasing resistance to further rapid expansion of bank loans. Through July, there was little evidence that this resistance was imposing any significant drag on growth of business loans. However, business loans at banks in major cities, which had increased during the first seven months of 1966 by an average $244 million per week, slowed down in the first three weeks of August to an average rise of less than $20 million (after seasonal adjustment).

There can be no objection to a Federal Reserve policy of limiting growth of total bank



Money Supply of the United States
Seasonally adjusted

Note: Demand deposits adjusted and currency outside banks, monthly averages of daily figures. Rate of change is annual rate of monthly change, 3-month moving average.

Source: Board of Governors of the Federal Reserve System.

credit and money supply today. Indeed, this *Letter* urged such a policy on numerous occasions in the last two years when growth of bank credit and money supply appeared excessive. Nevertheless, it must be pointed out that there are risks involved in concentrating on one kind of credit, such as business loans. As the article on prices in this issue suggests, it is not at all clear that business investment spending is the prime source of inflationary pressures in the economy. With manpower resources stretched taut, we are now unusually dependent upon productivity increases and growth in production facilities—both of which come largely from business investment—for restraining industrial prices.

Money Supply Down

Bank credit is but one of the channels through which the Federal Reserve authorities influence economic activity and prices. The other is the money supply. While changes in cost and availability of credit affect investment spending, recent research indicates that changes in the stock of bank deposits and currency available to the public have powerful effects upon consumer as well as business spending and on national income. As a matter of fact, some economists believe that changes in the rate of growth of money supply are among the chief causes of business fluctuations. For example, Professor Milton Friedman, reporting on the monetary studies of the National Bureau of Economic

Research in the Bureau's Forty-Fourth Annual Report said:

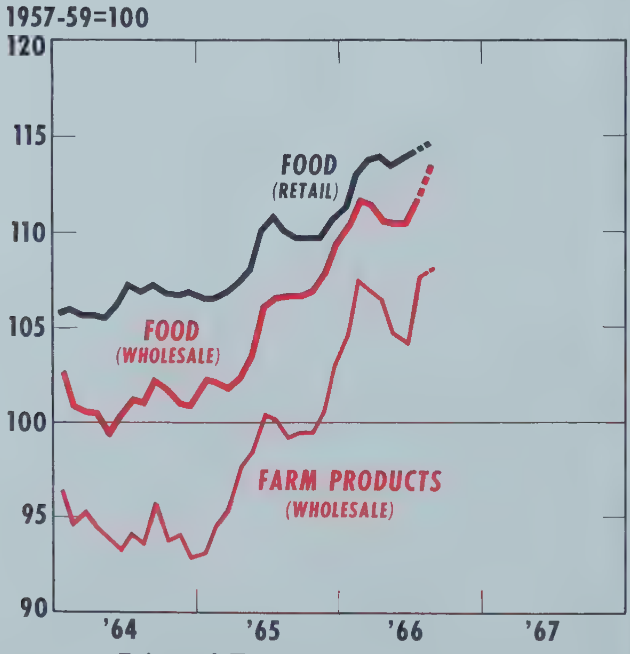
> Changes in the quantity of money have important, and broadly predictable, economic effects. Long-period changes in the quantity of money relative to output determine the secular behavior of prices. Substantial expansions in the quantity of money over short periods have been a major proximate source of the accompanying inflation in prices. Substantial contractions in the quantity of money over short periods have been a major factor in producing severe economic contractions. And cyclical variations in the quantity of money may well be an important element in the ordinary mild business cycle.

As can be seen from the chart on the preceding page, there has been a sharp slowdown in the rate of money supply growth since the end of last year, and an actual contraction in recent months. The apparent degree of success, or lack of it, in restraining business investment spending, therefore, should not be the test of Federal Reserve policies for restraining inflation. The reduction of money supply growth is potent medicine, whether or not the selective measures aimed at investment spending have noticeable results.

This is a time for patience in the application of monetary policy. Given the expectations engendered by the price inflation of the past year, there is no feasible combination of public policies that could bring the rise in prices to an immediate halt. The monetary authorities have moved in the right direction. They should, however, guard against being tempted by the persistence of price and wage increases into trying to do too much. A movement toward price stability will come gradually at best, and may already be under way.

Prices, Guideposts and Anti-Inflation Policy

Soaring food prices and the smashing of the 3.2 per cent wage guidepost in the airline strike settlement have aroused renewed alarm over inflation. Housewives this summer were shocked by sudden jumps in the cost of bread, milk, eggs, butter, and many fruits and vegetables on top of already high prices for pork and beef. The 5 per cent annual increase in wages and welfare benefits won by the machinists' union came as a stunning development to the business community. At the beginning of a new round of wage bargaining in major industries, the guidepost barrier had collapsed with the first volley from labor's big guns.



Prices of Farm Products and Foods at Wholesale and Retail

Source: U.S. Bureau of Labor Statistics.

Noting that steel sheet prices were raised 2.1 per cent during the height of the airline strike furor, many people concluded that the flood gates have been opened for runaway inflation. The news that the consumer price index through July had been rising at an annual rate of 3.5 per cent this year compared with a 1.7 per cent increase in 1965 seemed to confirm these fears.

Calls for additional anti-inflationary actions were immediately heard. A number of prominent economists called for increased tax rates to restrict private demand. The Federal Reserve made further moves to tighten credit, while Congress seemed to become more cautious about voting enlarged budget appropriations. On August 31, the White House revealed that the question of raising tax rates, including suspension of the investment tax credit, was under intensive study.

A More Flexible Guidepost Policy

The visible rise in inflationary fears is largely traceable to the progression of events during the 43-day airline strike. Public confidence was shaken by the inability of the President and Congress to prevent the machinists' union from gaining a wage settlement far in excess of the official wage guidepost while vastly inconveniencing the public and hurting many businesses dependent on air transportation. The claim of P.L. Siemiller, president of the machinists' union, that the new contract "destroys all existing wage and price guidelines now in existence"

and "completely shattered them for all unions" seemed uncomfortably close to the truth.

However, Chairman Ackley of the Council of Economic Advisers stated later that it represented a wage-fringe increase of 4.9 per cent a year and that it would not preclude further declines in airline fares because of the high rate of productivity growth in the industry. Airline sources put the cost at 5 per cent a year, after allowing for the cost-of-living escalator.

To the extent that the new outcry for tax increases is caused by fears engendered by the collapse of the guideposts, it may be based on a misapprehension about the effectiveness of the old guidepost policy.

Realistically speaking, the failure of the 3.2 per cent guidepost formula should not have come as a surprise. It had already been violated with impunity by many unions, most notably by the auto workers in November 1964 and by construction unions too numerous to mention. In a period of surging business activity, low unemployment rates and high food prices, the 3.2 formula stood little chance of acceptance against the demands of the major industrial unions, whose contracts are expiring this year and next.

But this does not mean the end of efforts to stabilize wages and prices in key industries. In fact, the groundwork for a new approach has already been laid by the President's Advisory Committee on Labor-Management Policy, whose report was issued on August 18.

This 21-man committee — evenly divided among representatives of business, labor, and the public—called for a return to the more flexible approach envisioned in the 1962 Annual Report of the Council of Economic Advisers, which had emphasized that the wage guidepost was *not* a "rule," *not* an "arbitrary guide," and *not* a "mechanical formula." While supporting "maximum efforts . . . through voluntary procedures" to keep wages and prices aligned with productivity growth in the economy, the panel maintained that "it is impractical if not impossible to translate the goals reflected in the guideposts into formulae for application to every particular price or wage decision."

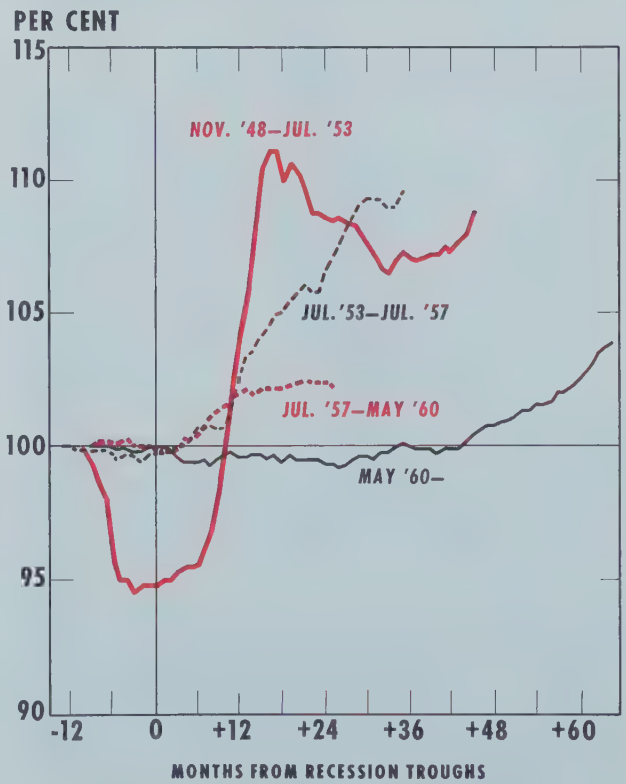
The committee, which includes George Meany and Walter Reuther of the AFL-CIO among its members, proposed to take a leading part in stabilization efforts. It recommended that whenever labor-management issues are the "apparent chief cause" of inflationary problems, the CEA should refer them to the Advisory Committee, which would recommend corrective action to the President. Though still in a formative stage, the new approach may well be more effective than the rigid formulas issuing from Administration economists.

What the Price Indexes Show

There is a danger of overreacting to increases in widely publicized price indexes. In fact, a dissection of the official price indexes indicates that most of the rises in prices have not been of the sort that are readily controllable by changes in demand without dangerous side effects.

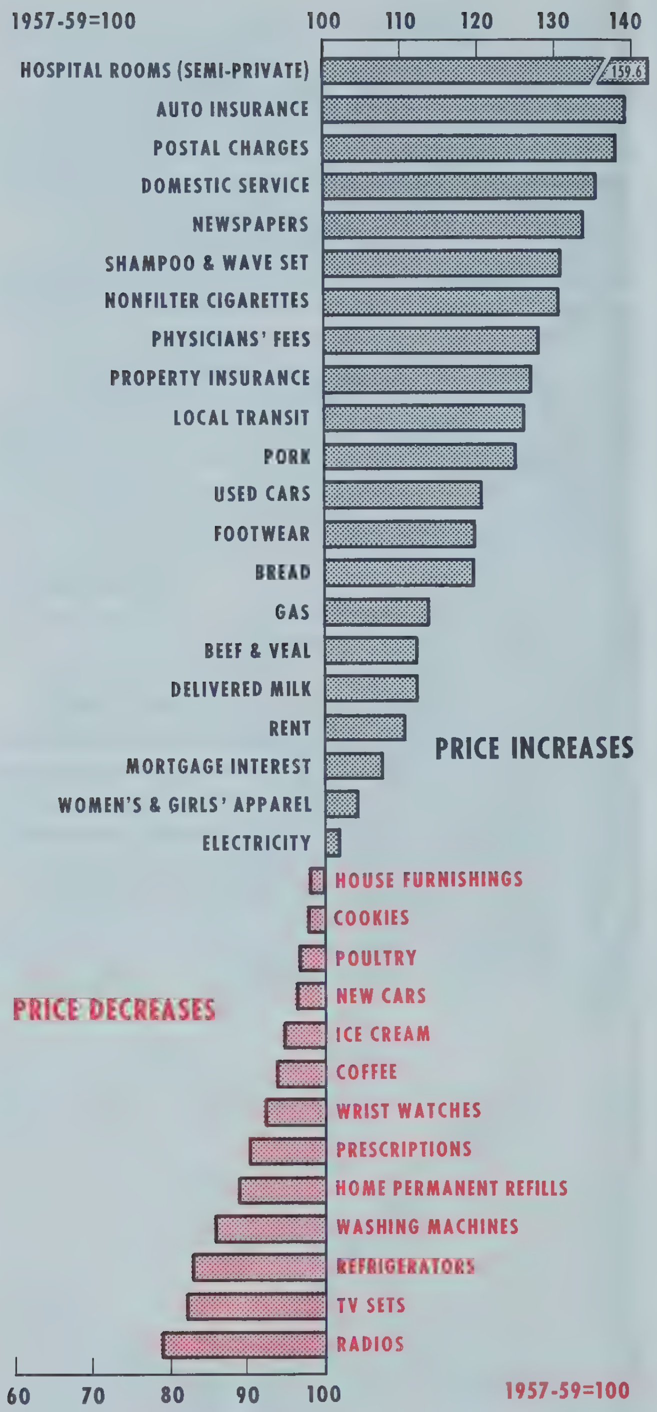
Thus, while the over-all wholesale price index (WPI) has climbed 6 per cent since July 1964, about 62 per cent of the total increase has been accounted for by three categories: farm and food products; nonferrous metals; and hides, skins and leather products. In all three areas, it takes considerable time for supplies to respond to changes in demand so that cyclically short supplies have resulted in steep upswings in prices. Farm and food products alone have accounted for nearly half of the total increase in the WPI, primarily owing to the downswing in cattle and hog supplies during 1965 and early 1966. With prices of cereals, feed grains, soybeans, dairy products and oil seeds also on an upswing, farm and food costs are still rising.

At the same time, industrial prices have been climbing since the fall of 1964 after five years of relative stability. As the accompanying chart shows, however, the rise of industrial prices has been a regular feature of business expansions since World War II. The flatness of the indus-



Movement of Wholesale Industrial Prices in Recent Business Expansions

Source: U.S. Bureau of Labor Statistics.



Changes in Selected Items in the Consumer Price Index from 1957-59 to June-July 1966

Source: U.S. Bureau of Labor Statistics.

trial price trend during the early stage of the current expansion was largely due to declining prices of raw materials and many intermediate materials, which in turn reflected worldwide over-capacity.

But now that supplies have begun to catch up with demand, particularly for copper, lead, zinc and cattle hides, raw material prices seem to have passed their peak. These factors, as well as a change in the system of cotton subsidies, have led to a downtrend in the costs of industrial materials. From a post-Korean war peak of 124.9 in mid-March, the BLS daily index of 13 industrial materials (1957-59=100) plunged 13 per cent to 108.7 in late August, the lowest level since September 1964.

The anatomy of consumer prices indicates that the rise of the over-all index is a far more complex phenomenon than ordinarily understood. As shown by the large chart, which depicts changes of selected items in the BLS consumer price index (CPI) since the 1957-59 base period, the uptrend has not been the result of simple profiteering or failure to pass on high productivity gains, as frequently charged.

Especially notable are the declines in many key durable goods—autos, housefurnishings, home appliances and television sets—produced in high-productivity industries. Import competition in such lines as radios and wrist watches has also benefited consumers.

On the other hand, the costs of staying in a hospital, hiring a maid, visiting a beauty parlor, or buying a newspaper are climbing sharply because wages are going up while productivity rises slowly if at all. Mounting costs of distribution and higher farm prices account for much of the rise for milk and bread, while increased state and local taxes have added much to the cost of cigarettes. The spread of health insurance, and more recently the Medicare program, have been straining available hospital facilities and encouraging higher physicians' fees.

More generous damages awarded by juries and judges—together with more accident-prone teenage drivers and higher car repair bills—have sent auto insurance costs soaring. The fact that some of the fastest-climbing items in the cost of living — hospital charges, local transit and postal services—are largely or wholly provided by government or by charitable organizations — belies the notion that profiteering by private business is a significant element in the rise of consumer prices. However, many improvements in quality—as reflected in the case of medical care in shorter hospital stays and longer average longevity—are immeasurable and are not allowed for in the CPI.

Policy Lessons from 1956-57

It is one of the ironies of postwar price history that plain bad luck on food prices has been a key factor in the current inflation scare as well as in the last one during 1956-57. The similarities and contrasts between the last year and a half — January 1965-July 1966 —

and the 1956-57 period are brought out in the accompanying chart. Since January 1965, the CPI has risen by 4 per cent—or 2.7 per cent a year—in contrast with a larger increase of 5.5 per cent—or 3.7 per cent a year—in the comparable period of January 1956-July 1957. Yet, in both periods, food prices rose by more than 7 per cent and accounted for roughly two fifths of the respective increases in over-all consumer prices. The costs of services rose by the same percentage—5.1 per cent—in both periods.

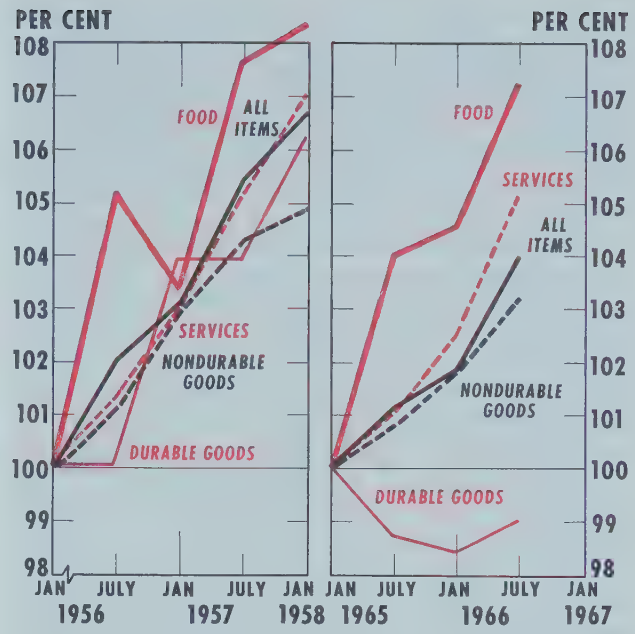
The rise in the CPI has been smaller this time because of the more moderate behavior of prices of nonfood consumer goods. Costs of nondurables (excluding food) have risen less than in 1956-57—3.4 per cent currently vs. 4.3 per cent in the earlier period. More important, prices of durable goods have fallen by 0.6 per cent over the last eighteen months, compared with a rise of 3.9 per cent in 1956-57. Though the lifting of Federal excise taxes was a factor in the recent decline, price tags on consumer durables, as noted earlier, have been decreasing for several years.

One of the key lessons offered by our 1956-57 experience is that an inflation largely attributable to food supply factors cannot be effectively suppressed by limiting over-all demand without creating even worse disruptions elsewhere in the economy. Thus, while monetary and fiscal policies were steadily tightened in 1956 and 1957, food prices continued to rise to a July 1958 peak 11 per cent above January 1956 even though the economy had slipped into a recession after July 1957.

Rather than affecting food prices, the demand-restricting measures hit sales of autos and other consumer durables. Because people must eat—and food habits change only slowly—households tend to pay the higher price for food while putting off postponable purchases of things like autos and appliances. In 1958, auto sales plummeted to 4.3 million cars for the sharpest peacetime contraction since 1938.

Restrictions on demand aggravated the cost-push inflation in that period. With the money supply held down to only a nominal increase between December 1955 and December 1957, over-all demand was too weak to permit industries to operate at efficient and profitable levels. As a result, the growth of nonfarm productivity suffered: output per manhour actually fell in 1956 and grew at a subnormal rate in 1957. The cost-push inflation of 1956 and 1957 largely reflected the efforts of business to relieve through higher prices the profit squeeze arising from steeply rising wages and negligible increases in productivity to pay for them.

The recession that began in August 1957, as



Changes in Consumer Prices by Major Categories, Jan. 1956-Jan. 1958 vs. Jan. 1965-July 1966

Source: U.S. Bureau of Labor Statistics.

well as the weakness of the subsequent recovery, is often ascribed to an excessive investment boom in 1956-57. But excess capacity at that time developed largely because money demand was not permitted to grow sufficiently to match the expanding supply capacity of industry.

Is Demand Excessive?

Economists calling for tax increases have stressed their belief that demand is already excessive and must be restricted in order to prevent prices and wages from spiraling upward. Federal Reserve Board officials have defended their recent credit-tightening moves as being made necessary by the absence of fiscal measures to check demand. Proposals for suspension of the investment tax credit are based on the belief that the capital investment rate is too high.

Any sensible person would agree that over-all economic demand should not be permitted to expand faster than our capacity to produce the goods and services needed. Owing to overly expansive fiscal and monetary policies earlier, it is undoubtedly true that demand was permitted to grow too rapidly in the latter half of 1965 and in early 1966. Some of the inflationary symptoms now showing up are actually the lagged effects of earlier policies.

But the present evidence does not support the idea that demand is now growing at an excessive rate. Real growth of GNP in the second quarter slowed to an annual rate of 2 per cent. The unemployment rate among experienced workers has risen since May.

As in 1956-57, advocates of additional demand-restricting measures may be confusing what is largely a food-and-services inflation with a general industrial-goods inflation. Moreover, they seem to be underestimating the real growth potential of the economy and neglecting measures to increase supply.

New estimates indicate that output per man-hour climbed at a rate of about 3.8 per cent a year in 1960-65—higher than previously believed—and that similar gains were made in first half 1966. Since the potential labor force is growing at about 2 per cent a year, the real growth potential of the economy may be expanding at a rate of about 5-5½ per cent a year. Allowing for a "normal" upcreep in measured prices of about 1-1½ per cent a year, the growth potential in money GNP terms may be rising by about 6-7 per cent a year. Thus, the economy can readily absorb the growing costs of Vietnam, which have been rising at a rate of about $2 billion a quarter.

The increasing growth potential of the economy can be attributed to high rates of capital investment, longer working hours, an increasingly better-educated labor force, rapid technological development, improved business management and Federal tax-reduction policy. The fact that people are working longer hours seems to reflect the improved incentives for earning extra income that resulted from the 1964-65 income tax cuts. Raising Federal income tax rates again—on top of higher Social Security and state and local taxes—would reduce the incentives for work while whetting demands for higher wages.

Restricting Demand vs. Boosting Supply

To restrain over-all demand to fit capacity, many Federal nondefense programs should be strictly limited now that unemployment is so low. Monetary policy also should restrict the expansion of the money supply to no more than what is needed for real economic growth.

But it is likely that inflation can be checked more effectively now by increasing supplies and encouraging productivity growth than by checking demand precipitously and suppressing individual movements of prices and wages. Under a more flexible stabilization policy, for example, wage increases exceeding the 3.2 per cent figure could be accepted provided that productivity increases are accelerated. From the standpoint of raising productivity, moreover, it would make little sense to discourage business from making capital investments by suspending the investment tax credit or raising corporate taxes.

Measures to enlarge the supply of physicians, nurses and other medical personnel are needed to check the soaring costs of medical care, which have accounted for 9 per cent of the increase in consumer prices this year. Intensified efforts to upgrade the skills of workers and young people, particularly through on-the-job training, would help relieve inflationary pressures in industry.

In light of the leading role played by food prices in the current inflation, measures to boost food supplies may be among the most effective anti-inflationary weapons now available. The key factor determining the level of food prices for 1967 and 1968 will be the supply of corn and other feed grains, which in turn will influence future supplies of meat and poultry. The present costly program to restrict corn acreage should be drastically eased.

Better still, we should take the opportunity now offered by strong world demand to free grain growers from restrictive programs altogether. Price-support and other farm programs threaten to destabilize the economy by pushing up food prices while providing little permanent help to farmers, particularly the younger farmers seeking to expand. In the new era of world food shortages, farmers should be able to earn higher net incomes from free markets.

Increased production and higher productivity can go a long way toward solving the problem of inflation. Too much time and energy is now being wasted in bickering over how to divide up the economic pie when a better answer is to bake a bigger pie.

World Trade Negotiations: A Progress Report

This month, after three years of disappointing progress, the major trading nations are resuming negotiations to expand international trade through reductions in tariffs and other barriers. The bargaining will, it is expected, move into high gear since the broad authority conferred upon the President of the United States by the Trade Expansion Act of 1962 to negotiate tariff cuts is scheduled to expire in June 1967. Under this authority, the President may reduce U.S. tariffs —on a reciprocal basis—by as much as 50 per cent over a period of five years.

The current round of bargaining—sometimes referred to as the Kennedy Round because of efforts made by the late President to launch this great venture in international cooperation—is the sixth in the twenty-year history of the General Agreement on Tariffs and Trade (GATT). Delicate and difficult matters must be dealt with in negotiations of great complexity and far-

reaching economic and political significance. Like an iceberg, these matters have, sometimes, more beneath the surface than above. They affect the vital, bread-and-butter interests of many countries, including all the principal trading nations other than Russia.

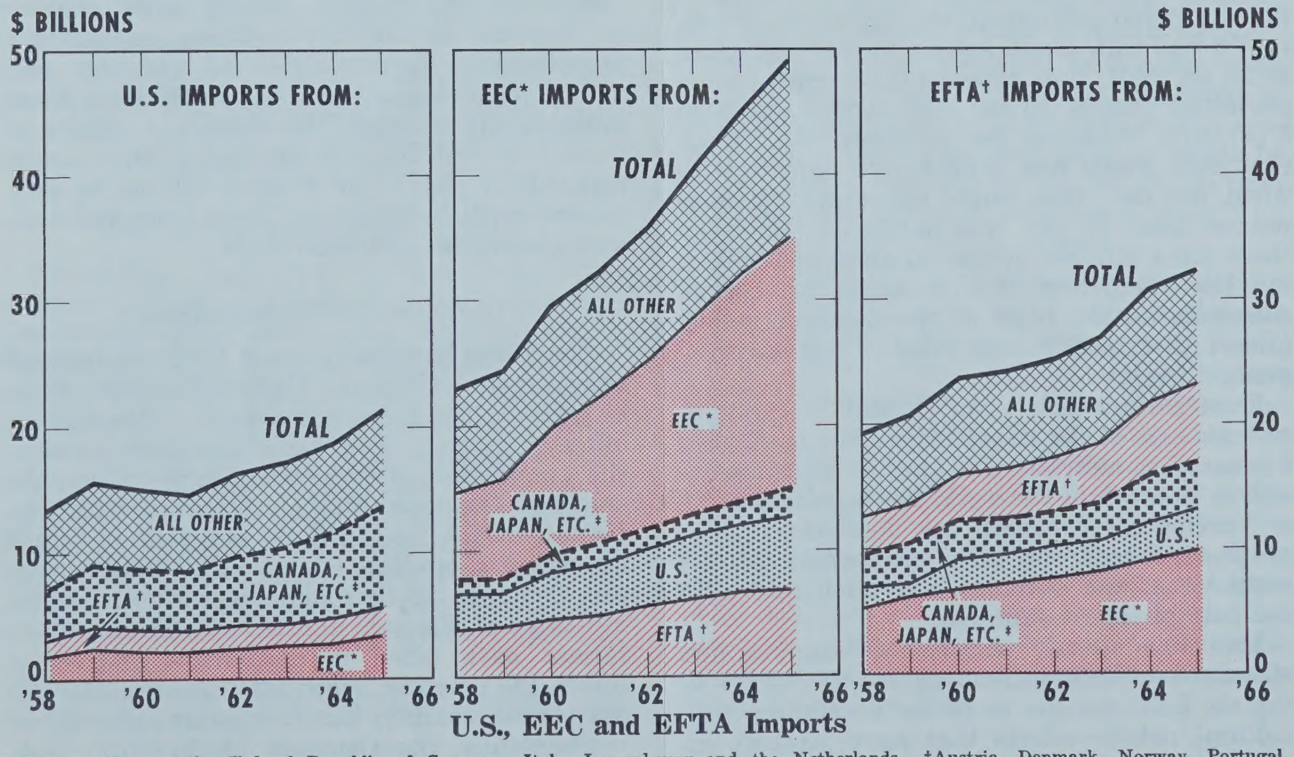
The negotiations began in the spring of 1963 but failed to proceed as rapidly as had been hoped. For one thing, reductions in obstacles to trade are sought over a greater range than ever before—tariffs as well as nontariff barriers—and aim at across-the-board tariff cuts rather than item-by-item concessions. And for another, one of the major negotiating partners, the European Economic Community (EEC), requires a unanimous vote of its six member nations to determine its policies; such decisions can be made only after lengthy and hard internal bargaining and are difficult to alter. In fact, it is only now that the European Common Market, having hammered out common agricultural price and marketing policies and a joint position on GATT trade negotiations, is able to bargain.

The Trade at Stake

While some 80 countries are participating in GATT negotiations, the bulk of bargaining is among Western European nations, the United States, Canada and Japan, with Australia, New Zealand and South Africa also taking part. Concession, for a given product, to one nation is, under the most-favored-nation principle, a concession to all. Full reciprocity, however, is not to be required of less-developed countries. This concept, embodying the recognition that the less-developed nations should not have to make reductions in their trade barriers that might be inconsistent with their development efforts, breaks new ground.

For the United States, these general considerations mean, in practical reality, that the negotiations concern primarily its imports from Western European and other advanced industrial countries. As shown in the chart, such imports represent approximately three fifths of total U.S. purchases abroad. The remaining two fifths come from the less-developed nations in Latin America, Asia and Africa; this includes many products that the United States imports duty-free. The EEC constitutes a large source of U.S. imports; but, as stands out from the chart, the nations grouped in the European Free Trade Association (EFTA), Canada and Japan also carry on a large trade with the United States.

The bargaining concerns a multitude of tariff schedules that, as is well known, are difficult to compare from one country to another. From such comparisons as have been made, it emerges that U.S. tariffs are dispersed over a wide range, the Common Market tariffs are the highest on



U.S., EEC and EFTA Imports

* Belgium, France, the Federal Republic of Germany, Italy, Luxembourg and the Netherlands. †Austria, Denmark, Norway, Portugal, Sweden, Switzerland and the United Kingdom. ‡Including also Australia, New Zealand and the Republic of South Africa.

Note: The imports likely to be affected by world trade negotiations are, approximately, those shown below the broken line.

Source: World Bank-IMF, *Direction of Trade.*

foods and the United Kingdom tariffs the highest on industrial goods; but the average levels of all three are of roughly similar heights. Reciprocal cutting makes, therefore, good sense.

The Pattern of Issues

On the industrial side, the governments have agreed upon a "working hypothesis" of a 50 per cent cut in tariffs. Understandably, each nation regards certain items as so sensitive to import competition that it will wish to offer only a lesser cut or none at all. These so-called "exceptions lists," tabled in 1964, are subject to multilateral "confrontation and justification." Their length and significance vary from country to country. The lists and the negotiations about them have been confidential; but, judging from newspaper comments on both sides of the Atlantic, the exceptions cover important segments of world trade in chemicals, steel products, aluminum, pulp and paper and textiles. As U.S. negotiators have publicly stated, the list of the European Common Market is overly large, particularly in relation to the lists submitted by the other principal countries.

Related to "exceptions lists" is the question of tariff "disparities"—items on which one country has a high tariff and another a low one. This question, raised by Common Market negotiators, aims at some of the high U.S. tariffs. The gist of the argument, highly simplified, is that an equal percentage cut across the board, say by one half, would leave a 40 per cent tariff at 20 per cent, thus allowing it to remain more protective than a 10 per cent tariff reduced to 5 per cent. Moreover, the countries with a 5 per cent duty would find little left to bargain with when, one day, they would try to get others to reduce their 20 per cent tariffs. In addition, there are a number of special problems, including the calculation of U.S. tariffs for certain chemicals on the basis of the domestic selling price rather than on the value of the imported product itself.

Even more sensitive and difficult is the agricultural side of the negotiations. For more than a generation, agriculture in the United States as well as in much of the world has been treated as a "special case." There are domestic support programs which, in turn, necessitate import restrictions; and surpluses are often sold with the help of export subsidies.

Into this already complex situation a new element has been introduced by the efforts of the six EEC nations to devise a common agricultural policy—efforts that have recently resulted in agreements to establish, by mid-1968, unified markets and prices, and price supports, for all important products. Presently, there is a wide range of prices within the EEC, with Germany having, for instance, the highest grain prices and France the lowest; the new price is in-between but far above the world price. To protect agriculture, imports from outside the EEC will be subject to variable levies; the proceeds, channeled into a common fund, are to be used to promote agricultural investment or subsidize exports. The system will tend toward making outside producers residual suppliers, able to sell in the Common Market only when output there falls short of demand.

The implementation of these policies is a matter of major importance to the United States, for the Common Market—buying as it does $1.5 billion worth of U.S. farm products annually—is the biggest single cash market for U.S. agricultural exports. It is a matter of great interest to countries like Australia, Canada, Denmark and New Zealand. Against this background, it is evident that trade negotiations that would not consider agricultural and industrial products together would be one-sided. Besides, the Common Market nations are obviously interested in access to U.S. and other markets for their manufactured goods.

Finally, nontariff barriers to trade will also be under scrutiny. In many countries, quotas hold down imports of some important products; Japan imposes "voluntary" export quotas and there is an international agreement to control the cotton textile trade. Among other barriers are customs valuation procedures, government procurement practices, internal taxation and antidumping regulations. As tariffs have been progressively reduced, the restrictive effects of these nontariff barriers are being increasingly realized. The hard core of them will not be easy to deal with because they have deep political, social, economic and fiscal roots.

The Need for Positive Results

The Trade Expansion Act of 1962 was tailored to expectations that the United Kingdom would be part of the European Common Market. It offered a formula that would have made possible the elimination of industrial tariffs where the enlarged Common Market, together with the United States, provided 80 per cent of world exports of a product, not counting trade within the Common Market and with Russia, other countries of Eastern Europe, etc. These expectations have failed to materialize and, as a result, the potential scope for trade negotiations has shrunk sharply; but it remains appreciable.

Meanwhile, the Common Market has made substantial progress toward becoming a customs union. Internal customs duties on industrial products within the Common Market have by

now been brought down to 20 per cent of their original level; a further 5 per cent reduction is to be made in July 1967 and the remaining 15 per cent is to be abolished a year later. The six are also adjusting their individual tariffs to the ultimate external tariff levels; this reveals many industrial items with rates higher than some members' pre-1958 rates. The EEC, however, finds it difficult to move toward a more fully integrated economic union.

As to EFTA nations, they are making no effort to go beyond a loose association. Internal tariffs on industrial goods were reduced by a further 10 per cent last January, with the remaining 20 per cent due to be abolished at the end of this year. The EFTA requires no common tariffs against outsiders.

The Common Market is thus establishing a new pattern in its world trading relationships. During the Community's formative years, the United States was openly and consistently aiding efforts toward European integration, partly for reasons of international security, partly in the expectation that the Common Market would be outward-looking in its trade policy and that a smaller slice of a larger pie spurred by economic growth of an integrated market would be better for outsiders than a larger piece of a smaller pie. In fact, the EEC has been expansionist and, in relation to outsiders, has removed industrial quotas and extended to them some of the tariff reductions that it has made among its members. As may be seen from the chart, Common Market imports from the United States have been increasing year in year out; but the U.S. share in total EEC imports has trended downward.

Regionalism and Multilateralism

All things considered, there is thus less assurance today than three years ago that the present trade negotiations will bring about substantial results. Press comments cite the possibility of 20-30 per cent cuts in industrial tariffs, spread over the next five years. With regard to farm products, they envisage a mere holding of the line, though the beginnings of world arrangements might be marked out; with mounting world food shortages, old problems may well reappear with a new face. However valuable the outcome of the negotiations may be, it will be less than what was—perhaps too confidently—expected.

Not too surprisingly, therefore, thought has been given to other approaches to freer trade. Should multilateralism suffer a setback, it is said, recourse could be had to regional solutions. Thus, a North Atlantic free trade area might be established, initially linking Canada, the United States and EFTA, but with an open door to the EEC and other industrially advanced nations, including Japan, Australia and New Zealand. The new grouping would commit members to lower gradually tariff and nontariff barriers on manufactured products. It might also offer concessions to Latin American and other less-developed nations if these countries adopt a clear course toward freeing trade among themselves through reductions in trade barriers that could later become effective also for imports from more-developed countries.

A North Atlantic free trade area along these lines might well be reckoned with as an alternative in the event that present trade negotiations were to produce but meager results because of difficulties of negotiating with the Common Market. Similarly, in such an eventuality, U.S. preferences might be established in favor of some Latin American exports, as Assistant Secretary of State Lincoln Gordon indicated recently at the meeting of the Inter-American Council of Commerce and Production at Mexico City. The objective would not be a permanent system of hemisphere preferences but rather a strategy to encourage other nations to join with the United States to give up preferential trade arrangements. The drawback is that increased regionalism might invite a reversion to divisive trade practices among nations. It might threaten to give renewed impetus to protectionism and economic nationalism. The chief casualty would be the principle of equal treatment, which has been the foundation for the remarkable growth of world trade over the past century.

The outcome of the forthcoming negotiations will thus have a major and, perhaps, decisive influence on the conduct of world trade. It will have a major direct impact on the future markets and profits of individual firms and industries. A successful round, providing for significant and balanced reductions in world trade barriers on a multilateral and fully reciprocal basis, will enlarge the scope of world trade. Perhaps even more important at a time when a steady progress toward freer trade and payments appears less assured than only a few years ago, a frank and constructive transatlantic dialogue will encourage the business community throughout the world.

FIRST NATIONAL CITY BANK

September 1966

PRINTED IN U.S.A.